(18)

No. 05-669
Title: BP America Production Company, Successor in Interest to Amoco Production Company, et al., Petitioners

v.

Rejane Burton, Acting Assistant Secretary, Land and Minerals Management, Department of the Interior, et al.

Docketed: November 25, 2005
Lower Ct: United States Court of Appeals for the District of Columbia Circuit
Case Nos.: (04-5006, 04-5007)
Decision Date: June 10, 2005
Rehearing Denied: August 24, 2005
Questions Presented

| ~~Date~~ | ~~~~~~~~Proceedings and Orders~~~~~~~~~~~~~~~~~~~~~~ |
|---|---|
| Nov 22 2005 | Petition for a writ of certiorari filed. (Response due December 27, 2005) |
| Dec 16 2005 | Order extending time to file response to petition to and including January 26, 2006. |
| Jan 19 2006 | Order further extending time to file response to petition to and including February 27, 2006. |
| Feb 23 2006 | Order further extending time to file response to petition to and including March 13, 2006. |
| Mar 13 2006 | Brief of respondents Rejane Burton, Acting Assistant Secretary, Land and Minerals Management, Department of the Interior, et al. filed. |
| Mar 13 2006 | Brief amicus curiae of Jicarilla Apache Nation on statute of limitations question only filed. |
| Mar 27 2006 | Reply of petitioners BP America Production Company, Successor in Interest to Amoco Production Company, et al. filed. |
| Mar 29 2006 | DISTRIBUTED for Conference of April 14, 2006. |
| Apr 17 2006 | Petition GRANTED limited to Question 2 presented by the petition. The Chief Justice and Justice Breyer took no part in the consideration or decision of this petition. |
| May 8 2006 | Extension of time within which to file the joint appendix and petitioners' brief on the merits to and including June 13, 2006. |
| May 19 2006 | Consent to the filing of amicus briefs in support of either party received from counsel for petitioners. |
| Jun 13 2006 | Joint appendix filed. |
| Jun 13 2006 | Brief of petitioners BP America Production Company, Successor in Interest to Amoco Production Company, et al. filed. |
| Jun 13 2006 | Brief amicus curiae of Mountain States Legal Foundation filed. |
| Jun 13 2006 | Brief amicus curiae of American Petroleum Institute filed. |
| Jul 14 2006 | Extension of time within which to file respondent's brief on the merits to and including August 4, 2006. |
| Jul 14 2006 | SET FOR ARGUMENT on Wednesday, October 4, 2006. |
| Jul 25 2006 | CIRCULATED. |
| Aug 2 2006 | Record received from U.S.C.A. for D.C. Circuit. (1 box) |
| Aug 4 2006 | Brief of respondents Rejane Burton, Acting Assistant Secretary, Land and Minerals Management, Department of the Interior, et al. filed. (Distributed) |
| Aug 4 2006 | Brief amici curiae of Jicarilla Apache Nation,et al. filed. (Distributed) |

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|---|---|
| Aug 4 2006 | Record received from U.S.D.C. for District of Columbia. (2 boxes) |
| Sep 7 2006 | Reply of petitioners BP America Production Company, Successor in Interest to Amoco Production Company, et al. filed. (Distributed) |
| Oct 4 2006 | Argued. For petitioners: Jeffrey A. Lamken, Washington, D.C. For respondents: Daryl Joseffer, Assistant to the Solicitor General, Department of Justice, Washington, D.C. |
| Oct 4 2006 | Joint Lodging received. (Distributed). |
| Oct 5 2006 | Lodging consisting of requested sample issue letters received from the Solicitor General. (Distributed). |

No. 05-705

Title: Global Crossing Telecommunications, Inc., Petitioner
v.
Metrophones Telecommunications, Inc.

Docketed: December 2, 2005
Lower Ct: United States Court of Appeals for the Ninth Circuit
Case Nos.: (04-35287)
Decision Date: September 8, 2005

Questions Presented

| Date | Proceedings and Orders |
|---|---|
| Nov 25 2005 | Petition for a writ of certiorari filed. (Response due January 3, 2006) |
| Jan 3 2006 | Brief of respondent Metrophones Telecommunications, Inc. in opposition filed. |
| Jan 11 2006 | Reply of petitioner Global Crossing Telecommunications, Inc. filed. |
| Jan 18 2006 | DISTRIBUTED for Conference of February 17, 2006. |
| Feb 21 2006 | Petition GRANTED limited to Question 1 presented by the petition. |
| Mar 20 2006 | Extension of time within which to file the joint appendix and petitioner's brief on the merits to and including May 22, 2006. |
| May 19 2006 | Joint appendix filed. |
| May 22 2006 | Brief of petitioner Global Crossing Telecommunications, Inc. filed. |
| May 22 2006 | Brief amicus curiae of AT&T filed. |
| May 22 2006 | Brief amicus curiae of Sprint Communications Company LP filed. |
| Jun 5 2006 | Extension of time within which to file respondent's brief on the merits to and including July 26, 2006. |
| Jul 14 2006 | SET FOR ARGUMENT on Tuesday, October 10, 2006. |
| Jul 17 2006 | CIRCULATED. |
| Jul 26 2006 | Brief of respondent Metrophones Telecommunications, Inc. filed. (Distributed) |
| Jul 26 2006 | Brief amicus curiae of the United Statesl filed. (Distributed). |
| Jul 27 2006 | Record received from U.S.C.A. for the 9th Circuit. (1 envelope) |
| Jul 27 2006 | U.S.D.C. for the Western District of Washington is electronically filed (no hard copy). |
| Aug 8 2006 | Motion of the Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument filed. |
| Aug 14 2006 | SET FOR ARGUMENT on Tuesday, October 10, 2006. |
| Aug 30 2006 | Reply of petitioner Global Crossing Telecommunications, Inc. filed. (Distributed) |
| Sep 1 2006 | Motion of the Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument GRANTED. |
| Sep 26 2006 | Supplemental brief of respondent Metrophones Telecommunications, Inc. filed. (Distributed) |
| Oct 10 2006 | Argued. For petitioner: Jeffrey L. Fisher, Stanford, Cal. For respondent: Roy T. Englert, Jr., Washington, D.C.; and James A. Feldman, Assistant to the Solicitor Generl, Department of Justice, Washington, D.C. (for United States, as amicus curiae.) |

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| Name | Address | Phone |
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Supreme Court, U.S.
FILED

No. 05-669

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IN THE

# Supreme Court of the United States

BP AMERICA PRODUCTION COMPANY AND
ATLANTIC RICHFIELD COMPANY,
*Petitioners,*

v.

REBECCA W. WATSON,
ASSISTANT SECRETARY OF THE INTERIOR FOR LAND
AND MINERAL MANAGEMENT, *et al.*,
*Respondents.*

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit**

## PETITION FOR A WRIT OF CERTIORARI

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## QUESTIONS PRESENTED

The Mineral Leasing Act of 1920 ("MLA"), 41 Stat. 437, codified as 30 U.S.C. § 181 *et. seq.*, provides for the payment of royalties on oil and gas from federal leases based on the "value of production removed or sold from the lease." 30 U.S.C. § 226(b)(1)(a). This case concerns the proper construction of that provision and the agency regulations promulgated thereunder. It also concerns the scope of the statute of limitations codified at 28 U.S.C. § 2415(a), which applies to "every action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract * * * ."

The questions presented are:

1. Whether the MLA, or the agency regulations promulgated thereunder, require lessors to pay royalties based on the value of production as determined at the leasehold location of production, or instead based on the enhanced value of production after it has been transported away from the lease and conditioned to a higher quality at off-lease treatment plants.

2. Whether—contrary to the decision below but consistent with decisions of the Tenth and Federal Circuits—the limitations period in 28 U.S.C. § 2415(a) applies to federal agency orders requiring the payment of money claimed under a lease or other agreement.

## LIST OF PARTIES AND PARTIES TO THE PROCEEDINGS BELOW

Petitioner BP America Production Company is the successor in interest to Amoco Production Company and Vastar Resources, Incorporated. Petitioner Atlantic Richfield Company, along with Amoco Production Company and Vastar Resources, Incorporated, were appellants in the court of appeals and plaintiffs in the district court.

Respondents are Rebecca W. Watson, in her capacity as Assistant Secretary of the Interior; Gale A. Norton, in her capacity as Secretary of the Interior; Southern Ute Indian Tribe; Assiniboine and Sioux Tribes of the Fort Peck Indian Reservation; Burlington Resources Inc.; Steve Westly, in his capacity as California State Controller; Jicarilla Apache Nation; the State of Colorado; and the State of New Mexico.

Respondent Norton was an appellee in the court of appeals and a defendant in the district court. She is the successor to Bruce Babbitt, who was also a defendant in the district court. Respondent Watson was an appellee in the court of appeals. She is the successor to Wallace P. DeWitt, who was a defendant in the district court. Assistant Secretary DeWitt was the successor to Sylvia V. Baca, who was also a defendant in the district court.

Respondent Southern Ute Indian Tribe was an intervenor supporting appellees in the court of appeals and an intervenor supporting defendants in the district court. Respondents Assiniboine and Sioux Tribes of the Fort Peck Indian Reservation; Burlington Resources Inc.; Steve Westly, in his capacity as California State Controller; Jicarilla Apache Nation; the State of Colorado; and the State of New Mexico, by and through the State of New Mexico Office of the Attorney General, were all intervenors supporting appellees in the court of appeals.

## CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.6 of the Rules of this Court, petitioners BP America Production Company and Atlantic Richfield Company state the following:

On December 31, 2001, Amoco Production Company and Vastar Resources, Inc. merged and formed BP America Production Company. BP America Production Company is wholly owned by BP Company North America Inc. BP Company North America Inc. is wholly owned by BP Corporation North America Inc. BP Corporation North America Inc. is wholly owned by BP America Inc. Atlantic Richfield Company is wholly owned by BP America Inc.

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IN THE

# Supreme Court of the United States

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BP AMERICA PRODUCTION COMPANY AND
ATLANTIC RICHFIELD COMPANY,
*Petitioners*,

v.

REBECCA W. WATSON,
ASSISTANT SECRETARY OF THE INTERIOR FOR LAND
AND MINERAL MANAGEMENT, *et al.*,
*Respondents*.

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**On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit**

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## PETITION FOR A WRIT OF CERTIORARI

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Petitioners Atlantic Richfield Company ("ARCO") and BP America Production Company—successor in interest to Amoco Production Company ("Amoco") and Vastar Resources Inc. ("Vastar")—respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

## OPINIONS BELOW

The opinion of the court of appeals (App., *infra*, 1a-20a) is published at 410 F.3d 722 (D.C. Cir. 2005). The opinion of the district court (App., *infra*, 21a-56a) is published at 300 F. Supp. 2d 1 (D.D.C. 2003). The September 12, 2000, decision of the Department of Interior's Minerals Man-

agement Service (App., *infra*, 68a-97a), MMS-97-0155-O&G; the March 24, 2000, decision of the Minerals Management Service (App., *infra*, 98a-126a), MMS-0063-O&G, MMS-97-0191-O&G; the February 26, 1998, decision of the Minerals Management Service (App., *infra*, 127a-143a), MMS-97-0315-O&G; the May 27, 1997, Minerals Management Service Letter Order to Amoco Production Company (App., *infra*, 144a-156a); and the January 22, 1997, Minerals Management Service Letter Order to Atlantic Richfield Company (App., *infra*, 157a-169a), are unreported.

## STATEMENT OF JURISDICTION

The judgment of the court of appeals was entered on June 10, 2005. The court of appeals denied a petition for rehearing on August 24, 2005 (App., *infra*, 175a). This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

## STATUTORY PROVISIONS INVOLVED

Relevant provisions of Section 17 of the Mineral Leasing Act of 1920, 41 Stat. 437, codified as amended at 30 U.S.C. § 226, are reprinted at App., *infra*, 176a-178a. Section 2 of the Act of July 18, 1966, Pub. L. No. 89-505, 80 Stat. 304, codified as amended at 28 U.S.C. § 2415, is reprinted at App., *infra*, 179a-182a.

## STATEMENT OF THE CASE

### I. Statutory and Regulatory Background

This case raises an issue of profound economic importance involving hundreds of millions of dollars—the proper method for measuring royalties owed to the government under the Mineral Leasing Act, as well as the proper construction of the statute of limitations governing actions for money damages for breach of contract.

#### A. Royalties Under The Mineral Leasing Act

1. The modern system of oil, gas, and mineral royalties—as the word "royalty" itself suggests—derives from the English feudal system. During the middle ages, the crown might grant the right to mine but "typically

reserved part of all the ore to be delivered 'on top of the ground free of charge,' which was also called 'royalty.'" John S. Lowe, *Defining the Royalty Obligation*, 49 SMU L. Rev. 223, 258 (1996). That in-kind payment was, by its nature, made at the mine. Although the crown had a right to a share of the valuable extracted materials, it did not have a right to any increase in value derived from further refinement of the materials or from their transportation to locations closer to the point of consumption. *Ibid.*

When private and public parties adopted royalty systems for oil and gas leases in the United States, they followed the same pattern. Leases requiring the payment of a portion of "'market value,' 'amount realized,' and 'market price' were used in royalty clauses * * * to describe a royalty *at the production point*, before the lessee applied its entrepreneurship to enhance value by transporting, processing or marketing the gas." Lowe, *supra*, at 259 (emphasis added).

2. When Congress adopted the Mineral Leasing Act ("MLA"), 30 U.S.C. § 181 *et seq.*, in 1920, it acted against the backdrop of that settled practice. Under the MLA, the Department of Interior ("DOI") issues and administers oil and gas leases for federal lands. 30 U.S.C. §§ 181-287. Lessees must pay the royalty established in the lease, but the royalty cannot be less than "12½ per centum in amount or *value of production* removed or sold *from the lease*." 30 U.S.C. § 226(b)(2)(A)(ii) (emphasis added). For at least the first 60 years following the MLA's enactment, the DOI and the Mineral Management Service ("MMS")—the division of the DOI responsible for collecting and verifying revenues due under the MLA—implemented Section 226 in accord with well-established royalty rules. In particular, the "value of production * * * from the lease" was measured "at the well." See *Indep. Petroleum Ass'n of America* v. *Armstrong*, 91 F. Supp. 2d 117, 125 (D.D.C. 2000), *rev'd in part, aff'd in part*, 279 F.3d 1036 (D.C. Cir. 2002); pp. 17-18, *infra*.

In 1988, the MMS revised its rules governing the valuation of gas from federal leases for royalty purposes. See *Revisions of Gas Royalty Valuation Regulations and Related Topics*, 53 Fed. Reg. 1230 (Jan. 15, 1988). Those regulations once again addressed the need to value production "from the lease" pursuant to the MLA when the production is *transported* to points of sale off the lease. *Id.* at 1257.[1] The rules codified the "DOI policy since 1961," which was "to grant transportation allowances when production is moved to a sales point off the lease in order to calculate *the value of the product at the lease.*" *Ibid.* (emphasis added). In other words, where the value of gas is enhanced by moving it away from the wellhead for sale, transportation related costs are deducted to derive the value of the gas at the wellhead. As the MMS explained:

> Where the value of gas has been determined * * * at a point (*e.g.*, sales point or point of value determination) off the lease, MMS shall allow a deduction for the reasonable actual costs incurred by the lessee to transport unprocessed gas, residue gas, and gas plant products from a lease to a point off the lease including, if appropriate, transportation from the lease to a gas processing plant off the lease and from the plant to a point away from the plant.

30 C.F.R. § 206.156(a) (1988). The rules confirm the agency's "past and present practice generally to allow," for royalty valuation purposes, cost adjustments that are "directly related to the transportation of lease production." 53 Fed. Reg. at 1261.

The MMS's 1988 rulemaking also codified the agency's "long standing policy that costs incurred to place production

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[1] While potentially confusing, the word "lease" in the oil and gas industry means either the "contract" or "agreement" providing for the right to extract, "or *the land area covered by that authorization*, whichever is required by the context." 30 C.F.R. § 206.151 (emphasis added).

in a marketable condition are to be borne solely by the lessee." 53 Fed. Reg. at 1243. As the MMS recognized in its notice of proposed rulemaking, that policy had been upheld by the D.C. Circuit in *California Co.* v. *Udall*, 296 F.2d 384 (1961). In that case, the D.C. Circuit affirmed the agency's interpretation of the phrase "value of production" to mean the value of gas conditioned to meet the quality requirements of the receiving pipeline at or within a short distance of the wellhead. See *Revisions of Gas Royalty Valuation Regulations and Related Topics*, 52 Fed. Reg. 4732, 4734 (Feb. 13, 1987).[2] By referencing quality standards at or near the wellhead, the decision in *California Co.* assured that royalty valuations would be determined—consistent with historic practice—at or in the immediate vicinity of the lease.

The 1988 rulemaking adopted the following marketable condition rule:

> The lessee is required to place gas in marketable condition at no cost to the Federal Government or Indian lessor unless otherwise provided in the lease agreement. Where the value established pursuant to this section is determined by a lessee's gross proceeds, that value shall be increased to the extent that the gross proceeds have been reduced because the purchaser, or any other person, is providing certain services the cost of which ordinarily is the responsibility of the lessee to place the gas in marketable condition.

30 C.F.R. § 206.152(i) (1988).

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[2] In the *California Co.* decision, the D.C. Circuit emphasized that—although the producer may be required to incur costs to condition the gas to meet the requirements of the receiving pipeline at or within a short distance of the well—the producer was not required to incur any transportation costs to move the gas "from the field in the neighborhood of the wells." *California Co.*, 296 F.2d at 387.

The regulations further defined "marketable condition." In the *California Co.* case, "marketable condition" was determined to be the quality standards specified by the producer's *wellhead* sales contracts. 296 F.2d at 387-88. Likewise, the MMS's 1988 regulations defined "marketable condition" as a condition "accepted by a purchaser under a sales contract typical for the field or area." 30 C.F.R. § 206.151. The definitions of the terms "field" and "area" reference the oil and gas producing reservoirs underlying the lease. *Ibid.* Consistent with *California Co.* and the "from the lease" requirement of the MLA, those definitions limited the "typical sales" to sales for the field or area in the immediate vicinity of the lease. *Ibid.*

**B. The Statute of Limitations**

This case also concerns the application of the six-year statute of limitations found at 28 U.S.C. § 2415(a). When Congress initially enacted the MLA in 1920, it did not include a limitations period for government actions to collect payments or royalties. In 1966, Congress enacted a six-year limitations period for government actions for money damages for breach of contract. Act of July 18, 1966, 80 Stat. 304, codified as 28 U.S.C. § 2415(a). That provision declares that "every action for money damages brought by the United States or an agency or an officer or agency thereof which is founded upon any contract * * * shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decision shall have been rendered in applicable administrative proceedings required by contract or by law, whichever is later."

Congress later amended Section 2415 to clarify its scope. See Section 9 of the Debt Collection Act of 1982, Pub. L. No. 97-365, 96 Stat. 1749, 1754, codified as 28 U.S.C. § 2415(i). Among other things, the amendments specify that "[t]he provisions of this section shall not prevent the United States or an officer or agency thereof from

collecting any claim of the United States by means of administrative offset, in accordance with section 3716 of title 31." *Ibid.*

## II. Factual Background

### A. Natural Gas Production in the San Juan Basin

This case concerns the production of natural gas commonly known as "coalbed" or "coalseam" gas, which is found in connection with coal formations. Compared to "conventional" natural gas (which is not produced in association with coal formations), most coalseam gas contains relatively high levels of carbon dioxide, only a marginal amount of "natural gas liquids," and little or no sulfur bearing compounds. C.A. J.A. 240. Because coalseam gas and conventional gas have different physical characteristics, the San Juan Basin has separate gas gathering and treatment systems to handle the large volumes of coalseam methane production. *Id.* at 256.

Coalbed gas, like conventional gas, is typically sold by the producers to affiliated and non-affiliated purchasers at or near the wellhead. C.A. J.A. 193. The wellhead purchasers may consume the coalbed production themselves in local residential, commercial and industrial applications; they may transport the production to downstream delivery points; or they may resell the production to various marketers or consumers at delivery points along the pipeline system. *Ibid.*

Most of the coalbed gas production that is not consumed in local markets near the production area is transported to off-lease facilities and treated into a finished condition necessary to meet quality standards for long-distance transportation by mainline pipelines. C.A. J.A. 257. Owners of coalbed production destined for mainline transportation to distant markets pay a fee for the transportation of the production from the wellhead points of production on the lease, through gathering pipeline systems, to off-lease treatment facilities. *Ibid.* At these off-lease facilities, the

gas is treated to reduce the carbon dioxide content to meet the quality requirements of downstream, high-pressure, mainline pipelines. *Ibid.* Those quality standards are more stringent than the standards of pipelines that gather gas at the well. The less stringent quality standards of wellhead gathering systems are typically incorporated by wellhead gas sales contracts that establish the quality standards producers must meet.

**B. The 1996 Dear Payor Letter**

Until the events giving rise to this case, San Juan Basin production that met the quality requirements of typical wellhead sales contracts was considered to be in marketable condition, without regard to whether the production was consumed in untreated condition in local markets or later treated to meet the more stringent quality standards of mainline pipelines used to transport gas to distant markets. The costs incurred to transport untreated production over gathering systems to the off-lease treatment facilities, and the treatment costs incurred to meet the transportation requirements of mainline pipelines, were regarded as deductible transportation costs, not costs incurred to put the production in marketable condition to be borne solely by the producers.

On April 22, 1996, the MMS issued a "Dear Operator/ Payor" Letter to producers of coalbed methane gas in the vicinity of New Mexico's San Juan Basin. App., *infra*, 170a-174a. The 1996 Payor Letter provided new "guidelines" to producers on how to report and pay royalties on coalbed methane. *Id.* at 170a. For the first time, the government claimed a royalty entitlement based on the *enhanced* value of coalbed methane *after* transportation to downstream treatment facilities and treatment in those facilities to meet mainline pipeline quality requirements. *Id.* at 170a-171a. The 1996 Payor Letter asserted that, for royalty purposes, the coalbed methane's "value" cannot be reduced to account for the costs of placing it in marketable condition, and that

the coalbed methane was not in marketable condition until it was transported to and treated in gas treatment plants to meet the quality specifications of mainline pipelines. *Ibid.*

That 1996 Payor Letter had two consequences. First, for any sales of untreated gas at the wellhead (*i.e.*, at the lease), some of the downstream costs of transporting the gas to the treatment facilities and all of the costs of treatment had to be *added* to the proceeds of the sales on untreated gas to determine the government's royalty value. Second, for sales of treated gas away from the lease, some of the costs of transporting and all of the costs of treating the gas could *not be deducted* so as to calculate the value of the gas at the lease. App., *infra*, 171a-173a. By requiring the addition of downstream transportation and treatment costs to proceeds for wellhead sales of untreated gas at the lease, and by disallowing the deduction of such costs from proceeds received for sales of treated gas downstream from treatment facilities, the government required the payment of royalties based on a value that *exceeds* the actual value of the production *at the lease*.

**C. Agency Proceedings**

1. On May 27, 1997, the MMS issued an order ("Amoco MMS Order"), directing Amoco to pay additional royalties based on an audit determining that Amoco had not computed royalties in accordance with the 1996 Payor Letter. App., *infra*, 144a-156a. On September 12, 2000, the Assistant Secretary of the DOI issued a decision ("Amoco Decision") denying in most respects Amoco's appeal of the Amoco MMS Order. App., *infra*, 68a-97a. Applying the requirements set forth in the 1996 Payor Letter, the Amoco Decision concluded that—even though coalseam methane was in fact commonly marketed at the lease under wellhead sales contracts—the production was not in marketable condition "prior to its subsequent treatment and transportation for use in distant markets." *Id.* at 78a. In its decision, the agency articulated a new "primary or

dominant end-use market" test for determining when gas is in "marketable condition":

> The question requiring resolution is whether the production sold at the wellhead is in marketable condition prior to its subsequent treatment and transportation for use in distant markets. In other words, is the market at the wellhead the primary market for the gas as opposed to the more distant market?

*Ibid.* Based on that new test, the Assistant Secretary created a new definition of "marketable condition": "I find that the mainline transporters' $CO_2$ quality requirements effectively establish a marketable condition standard for gas sold from the field or area." *Id.* at 82a-83a. In effect, the 1996 Payor Letter and the Amoco Decision declared that the definition of "marketable condition" would not be the "condition that the gas would be accepted by a purchaser under a sales contract typical for the field or area" near the lease. 30 C.F.R. § 206.151; App., *infra*, 187a. Instead, there would be a *per se* rule that equates "marketable condition" with the stringent quality standards of downstream interstate pipeline systems and dominant end-use markets. App., *infra*, 96a. The Amoco Decision also concluded that the Amoco MMS Order did not violate the six-year statute of limitations set forth at 28 U.S.C. § 2415(a). *Ibid.*

2. On March 24, 2000, the Assistant Secretary applied the same marketable-condition rule to ARCO/Vastar. App., *infra*, 98a-126a. Although ARCO/Vastar had presented evidence of sales of untreated coalbed methane in the production area, the Assistant Secretary ruled that the "dominant" market for gas from the area is distant end-use markets served by interstate mainline pipeline systems. App., *infra*, 104a.

On February 27, 2001, the agency denied ARCO/Vastar's petition for reconsideration of the March 24, 2000 decision. App., *infra*, 59a-67a. The agency again stated that "[m]ar-

ketability is determined in part by whether the production is satisfactory for use by those who ultimately purchase it for use." *Id.* at 64a. The agency therefore refused to accept the condition of untreated coalseam methane commonly sold under wellhead contracts as satisfying the marketable condition rule. *Id.* at 66a. The agency reasoned that "[s]ale-for-resale transactions [at or near the wellhead] * * * are not particularly informative regarding the actual marketability of the product" because much of the gas is subsequently treated and resold in distant downstream markets. *Id.* at 63a.

**D. The District Court's Decision**

Amoco and ARCO/Vastar sought review in the United States District Court for the District of Columbia, and the parties filed cross-motions for summary judgment. On November 14, 2003, the district court denied the motions for summary judgment filed by Amoco and ARCO/Vastar and granted the government's cross-motion. App., *infra*, 21a-56a. Although the district court characterized the agency's decisions as "somewhat circuitous," the court nevertheless affirmed the agency's rule that reducing the carbon dioxide levels of coalbed methane production was required to place the production in "marketable condition" because most of the gas would ultimately be transported to distant end-use markets. *Id.* at 32a. Accordingly, the district court held that the quality requirements applicable to mainline pipelines, used to transport gas to distant markets, effectively established the marketable condition standard for gas at the lease. *Id.* at 45a.

The district court also addressed whether the statute of limitations set forth in 28 U.S.C. § 2415(a) foreclosed the agency from collecting royalties due more than six years before the May 27, 1997, MMS Order. App., *infra*, 48a-55a. The court acknowledged a significant split of authority on whether Section 2415(a)'s limitations period applies to administrative proceedings before an agency, or instead is

limited to the filing of actions in court. *Id.* at 52a. Rejecting the Tenth Circuit's en banc decision in *OXY USA, Inc.* v. *Babbitt*, 268 F.3d 1001 (2001), and instead following *Samedan Oil Corp.* v. *Deer*, No. 94-2123, 1995 WL 431307 (D.D.C. June 14, 1995), *rev'd on other grounds*, *Indep. Petroleum Ass'n of America* v. *Babbitt*, 92 F.3d 1248, 1260 (D.C. Cir. 1996), the district court concluded that the statute of limitations in 28 U.S.C. § 2415(a) does not apply to agency efforts to impose and collect additional royalties and associated interest through agency proceedings. *Id.* at 55a.

**E. The D.C. Circuit's Decision**

Amoco and ARCO/Vastar appealed, and the D.C. Circuit affirmed. App., *infra*, 1a-20a.

1. Addressing the royalty valuation issue first, the D.C. Circuit acknowledged at the outset that it is possible to interpret the phrase "value of the production from the lease" in the MLA as referring to the value of production at the lease, *i.e.*, the value as the gas typically would be sold at the wellhead. App., *infra*, 8a. But the court concluded that it was reasonable for the MMS to read the phrase more broadly. *Ibid.* Specifically, the D.C. Circuit reasoned that "from the lease" could be construed as referring simply to the production's point of *origin*. *Ibid.* Under that construction, the "value of the production * * * from the lease" could mean production that originated from the lease, but valued at and after conditioning in locations other than the lease—in this case the enhanced value of treated production at off-lease treatment facilities. In so holding, the D.C. Circuit did not address the longstanding rule—both before and after the MLA's enactment—that royalty valuations are to be determined at the lease or the wellhead point of production.

The D.C. Circuit also rejected the contention that the MMS's new construction of the marketable condition rule conflicted with the agency's 1988 regulations. App., *infra*,

9a-10a. Those regulations, the D.C. Circuit agreed, defined gas in "'marketable condition' as gas acceptable to 'a purchaser under a sales contract typical for the field or area.'" *Id.* at 9a (citing 30 C.F.R. § 206.151). But the court accepted the MMS's view that, because much of the gas would eventually be treated and *resold* for use in distant markets, sales for such "*treated* gas were typical for the area, while those for untreated gas were not." *Ibid.* (emphasis in original). The court of appeals reasoned that neither the definition of "field or area" nor the requirement of "marketable condition" contained an express geographic limit. *Id.* at 10a. That conclusion, the court further reasoned, was bolstered by the agency's provision of transportation allowances for moving gas off the lease, which necessarily assumes "that valuation of gas 'at a point (e.g., sales point or point of value determination) off the lease' is permissible." *Ibid.*

2. Finally, the D.C. Circuit upheld the district court's holding that the statute of limitations found at 28 U.S.C. § 2415(a) does not apply to orders assessing additional royalties. App., *infra*, 16a-20a. The D.C. Circuit reasoned that, because the statute of limitations by its terms precluded any "action for money damages" unless "the *complaint* is filed within six years after the right of action accrues," the limitations period applies only to "a suit in a court of law," and not to "an agency enforcement order that happens to concern money due under a statutory scheme." *Id.* at 16a-17a (emphasis added).

The D.C. Circuit acknowledged that its holding rendered a portion of the statute wholly superfluous. App., *infra*, 17a-18a. In particular, Section 2415(i) created an exception to the limitations period for agency efforts to collect debts "by means of administrative offset"; that exception would be wholly unnecessary if the limitations period did not apply to administrative agency actions in the first place. *Id.* at 17a-18a. For that very reason, other courts of appeals—

invoking the rule that statutes should not be construed to render any portion superfluous—had interpreted Section 2415(a) as extending to administrative actions as well as actions filed in court. *Ibid.* (citing *OXY USA* v. *Babbitt*, 268 F.3d 1001 (10th Cir. 2001) (en banc) and *United States* v. *Hanover Ins. Co.*, 82 F.3d 1052 (Fed. Cir. 1996)). But the D.C. Circuit disagreed with the reasoning of those decisions. *Id.* at 19a. Instead, largely following the dissenting opinions in those cases, the D.C. Circuit ruled that Section 2415(a) does not apply to agency proceedings, including those seeking money under a contract. *Id.* at 19a-20a.

## REASONS FOR GRANTING THE PETITION

The court of appeals' decision in this case upholds agency orders that re-interpret the Mineral Leasing Act ("MLA"), as well as Mineral Management Service ("MMS") regulations—re-interpretations that would impose hundreds of millions of dollars of additional royalty obligations on pre-existing leases. Under those rulings, these gas producers no longer pay royalties based on the value of extracted gas at the wellhead (*i.e.*, "at the lease"). Instead, they now must pay royalties on the *greatly enhanced* value that extracted gas has *after* it is sold to purchasers, removed from the lease, transported to off-lease treatment plants, and processed to the finished quality necessary for transportation over high-pressure, mainline pipelines to distant end-use markets. That interpretation is inconsistent with the plain text of the MLA, because it requires royalty payments in excess of the "value of production removed or sold from the lease." It is contrary to the long-standing construction of similar royalty provisions and traditional practice for centuries before the MLA's enactment and half a century after. And it is inconsistent with the decisions of other courts, which recognize that the "value of production removed or sold from the lease" requires production to be valued *at the lease*, not at off-lease locations after the

production has been enhanced in value by putting it into finished condition.

The D.C. Circuit's decision also creates an express and irreconcilable conflict on the proper construction of the 28 U.S.C. § 2415(a). Many courts of appeals have held that Section 2415(a)'s limitations period for "action[s] for money damages brought by the United States or an officer or agency thereof * * * founded upon * * * contract" extends to *administrative* orders seeking additional money allegedly due under a lease or other agreement. *OXY USA, Inc.* v. *Babbitt*, 268 F.3d 1001, 1009 (10th Cir. 2001) (en banc) (holding that Section 2415(a) governs MMS orders assessing additional royalties); *United States* v. *Hanover Ins. Co.*, 82 F.3d 1052, 1055-56 (Fed. Cir. 1996) (holding that Section 2415(a) governs Customs Service actions to enforce a claim for antidumping duties); see also *United States* v. *Suntip Co.*, 82 F.3d 1468, 1476 (9th Cir. 1996) (applying Section 2415(a) to require the government to "submit th[e] claim to a contracting officer within six years of accrual"). Expressly disagreeing with the holdings of those cases—and adopting the reasoning of the dissenting opinions—the D.C. Circuit held that Section 2415(a) does not apply to administrative orders for the payment of money due under a contract. That square conflict in circuit authority warrants this Court's review.

## I. The D.C. Circuit's Construction Of The MLA Is Inconsistent With The Statutory Text And The Decisions Of Other Courts

### A. The D.C. Circuit's Decision Departs From The MLA's Plain Meaning And The Construction Adopted By Court After Court

The MLA provides that lessees shall pay royalties of not less than 12.5 percent "in amount or value of the production removed or sold *from the lease*," 30 U.S.C. § 226(b)(1)(A) (emphasis added), *i.e.*, from "the land area covered by" the lease, 30 C.F.R. § 206.151. Naturally read, that language

requires royalties to be determined as a percentage of the value of the gas at a geographic point *before* the gas leaves the lease property. The royalty is measured as a percentage of the "amount of" gas "removed," or of the value of the gas "sold," "from the lease." The royalty is *not* measured as a percentage of gas "removed" or sold "from" an unspecified off-lease location, after being finished in a treatment facility many miles downstream.

That natural reading of the statutory language reflects centuries-old understandings. Long before the MLA's enactment, in-kind royalties owed to the crown in England (*e.g.*, in the form of ore) were deposited above ground at the place of extraction. John S. Lowe, *Defining the Royalty Obligation*, 49 SMU L. Rev. 223, 258 (1996). In this country, gas royalty agreements followed the same pattern: Contracts calling for the payment of a portion of the "'market value,' 'amount realized,' and 'market price' were used in lease royalty clauses * * * to describe a royalty *at the production point*, before the lessee applied its entrepreneurship to enhance value by transporting, processing or marketing the gas." *Id.* at 259 (emphasis added). Indeed, for more than half a century after the MLA's enactment—until the decision in this case—courts have adhered to that same rule, calculating royalties as a percentage of the value of the gas at the point of production from the lease, *before* being removed from the property and treated at off-lease facilities. See p. 18, *infra* (citing cases).

Departing from that centuries-old understanding, the D.C. Circuit in this case reasoned that gas "removed or sold from the lease" can be construed as gas that has its "origin" in the lease region. App., *infra*, 8a. Accordingly, the D.C. Circuit ruled that royalties may be calculated as a percentage of the value of gas *not* as it exists at the leasehold site of production, but instead as a percentage of the enhanced value of the gas *after* it is removed from the property and processed to a different condition at distant

treatment facilities. *Id.* at 8a-9a. Even if one sets aside (for the moment) the impossibility of reconciling that construction with the agency's regulations, see pp. 20-23, *infra*, it defies text, history, and common sense. As a matter of text, that construction fails to assess royalties on the value of "production removed or sold from the lease." Instead, it assesses royalties based on the enhanced value of treated production removed or sold *from off-lease treatment plants*. As a matter of history, it departs from the centuries-old practice of measuring value at the lease—not at off-site locales after the resource has been improved to finished quality to enhance its value.

Finally, the construction defies common sense. Natural resources often are improved in quality and increased in value through later downstream processes prior to final consumption. But that does not mean that the government, when it agrees to accept royalties based on the value of the production taken "from the lease," is entitled to base royalties on the value of the finished good to which production is later converted. The fact that oil from a particular field may be used primarily to make gasoline does not mean that the government is entitled to a percentage of the value of the gasoline. Instead, the government is entitled to royalties on the value of the resource as it customarily exists when alienated at the lease—not the finished form it acquires miles away, after being sold to others and converted into a quality suitable for different end-use markets. Indeed a producer that sells its gas production at the wellhead (at the lease) under a typical contract will have no knowledge whether the gas will be consumed in the condition sold at the wellhead, or improved in quality and resold into different markets.

It therefore comes as no surprise that court after court has construed the MLA to require royalties to be a percentage of value at the lease—at the point of production—not after improvements in quality at a point off

the lease. See *United States* v. *Gen. Petroleum Corp.*, 73 F. Supp. 225, 254 (S.D. Cal. 1947) ("Natural-gas royalties are payable on the gas as it is produced *at the well.* It is the value of that gas which must be determined.") (emphasis added), *aff'd Continental Oil Co.* v. *United States*, 184 F.2d 802, 820 (9th Cir. 1950) (royalties are "calculated * * * values *at the wells*") (emphasis added); *California Co.* v. *Udall*, 296 F.2d 384, 387 (D.C. Cir. 1961) (royalties due on production within a short distance of the wells, such that the costs of moving the gas from the neighborhood of the wells is not includable in the government's royalty); see also *Marathon Oil Co.* v. *United States*, 604 F. Supp. 1375, 1386 (D. Alaska 1985) (holding that "value of production" requires "that royalties be based on the value of production *at the lease*") (emphasis in original), aff'd 807 F.2d 759, 765-66 (9th Cir. 1986); *Indep. Petroleum Ass'n of America* v. *Armstrong*, 91 F. Supp. 2d 117, 125 (D.D.C. 2000) ("The longstanding interpretation of 'value of production,' one recognized by Interior (at least until the present matter) and affirmed by the courts, is that it refers to the value of oil or gas *at the wells*") (emphasis in original), rev'd in part, aff'd in part, *Indep. Petroleum Ass'n of America* v. *DeWitt*, 279 F.3d 1036 (D.C. Cir. 2002). The D.C. Circuit's conclusion that the MLA does not require royalty valuations to be determined "at the well" or "at the lease" cannot be reconciled with that longstanding body of precedent.

### B. The Decision In This Case Departs From Decades Of Precedent and Practice

Nor does the MMS' extra-statutory "marketable condition" requirement support the decision below. In the previously leading *California Co.* decision, the D.C. Circuit adopted the quality standards in wellhead gas sales agreements as the applicable marketable condition standard. 296 F.2d at 387. Likewise here, the quality standards in wellhead gas sales contracts should set the marketable condition standard. After all, the gas is typically *sold* at the

wellhead. That *sale* establishes the fact that the gas is sold in *marketable* condition.

Distinguishing *California Co.* and similar precedents, the decision below declared that "all the gas at issue [in *California Co.*] 'was conditioned by the seller and delivered to the purchaser within a short distance of the wells,' so the question presented here"—whether to base royalties on the gas's value at the wellhead or after treatment off-lease—"did not arise." App., *infra*, 8a. But that fails to distinguish *California Co.* Here, no less than in *California Co.*, virtually *all* of the production is sold and delivered "to the purchaser" under wellhead sales contracts. *Id.* at 4a ("producers sold untreated gas at the wellhead to purchasers who would pipe the gas to treatment centers"); *id.* at 9a (acknowledging the issue is the value of "production sold at the wellhead"). Here, as in *California Co.*, the production is initially conditioned to meet the quality requirements of the receiving pipelines at or near the wellhead consistent with wellhead sales agreements. C.A. J.A. 181-83, 258. Consequently, here, as in *California Co.*, the costs incurred to place production in that on-lease marketable condition are properly included in the government's royalty—but *only* insofar as the production was "conditioned by the seller and delivered to the purchaser in the field within a short distance of the wells." 296 F.2d at 387. The fact that the *purchaser* might later process the gas further and move it to distant markets is irrelevant. Indeed, *California Co.* clarified that "costs incurred in moving gas *from* the field in the neighborhood of the wells" are *not* "includable in the royalty base." *Ibid.* (emphasis added). The same is true of the off-lease transportation and treatment costs at issue here.

The only difference between this case and *California Co.* is the agency's demand for royalties. Here, but not in *California Co.*, the agency has decided to *disregard* the value of the gas as sold under typical contracts by

producers near the wellhead. Instead, the agency insists on calculating royalties based on a percentage of the gas's value when it is *resold* after further off-site conditioning to meet the more stringent requirements for distant transport on mainline pipelines. That approach cannot be reconciled with *California Co.*; it cannot be reconciled with the historical practice of valuation at the lease; and it cannot be reconciled with the statutory text, which requires the payment of a percentage of the gas "removed from" or "sold * * * from the lease," not the gas "sold from" off-site facilities after treatment to meet stringent mainline pipeline requirements for transportation to distant end-use markets.

### C. The D.C. Circuit's Decision Is Contrary To The Agency's Expressed Intent And Renders The Agency Regulations Internally Inconsistent

The decision in this case, moreover, upholds an agency construction that is inconsistent with the agency's own expressed intent, and places the agency's regulations at war with themselves. In various contexts, MMS has made it clear that it calculates royalties based on the value of gas at the lease. Nowhere did the agency explain why "production * * * from the lease" means production as sold at the lease in some contexts, but production as sold elsewhere for others.

1. The MMS's rules for calculating transportation cost allowances could not be more clear: Production is valued based on the gas's value at the lease, not based on its value off the lease. See *Revisions of Gas Royalty Valuation Regulations and Related Topics*, 53 Fed. Reg. 1230, 1257, 1261 (Jan. 15, 1988). As the D.C. Circuit noted below, the transportation allowance regulations "assume that valuation of gas 'at a point (e.g., sales point or point of value determination) off the lease' is permissible." App., *infra*, 10a. That valuation, however, is then *adjusted* for transportation costs to make sure it reflects the *value at a point on the lease*: "MMS shall allow a deduction for the reasonable

actual costs incurred by the lessee to transport [production] * * * from a lease to a point off the lease." 30 C.F.R. § 206.156(a) (emphasis added). The preamble to those 1988 regulations makes clear that the transportation allowance ensures that royalties are calculated as a percentage of value *at the lease*. 53 Fed. Reg. at 1230. It was the MMS's "policy since 1961 to grant transportation allowances when production is moved to a sales point off the lease *in order to calculate the value of the product at the lease*." *Id.* at 1257 (emphasis added). Similarly, in a more recent rulemaking, the MMS observed that "[s]ales away from (or 'downstream' from) the lease often are the *starting point* for determining royalty value, and the costs of transportation always have been allowed *in order to ascertain value at or near the lease*." See *Establishing Oil Value for Royalty on Federal Leases*, 65 Fed. Reg. 14022, 14029 (March 15, 2000) (emphasis added).

The 1988 regulations addressing the so-called "net-back" or "work-back" method for calculating the value of gas at the lease follow a similar approach. When the gas is sold or valued in markets downstream from the lease, those regulations require adjustments to calculate royalties as a percentage of the value at the lease:

> Net-back method (or work-back method) means a method for calculating market value of gas *at the lease*. Under this method, costs of transportation, processing, or manufacturing are deducted from the proceeds received for the gas * * * or from the value of the gas * * * at the first point at which reasonable values for any such products may be determined * * * to ascertain value *at the lease*.

30 C.F.R. § 206.151 (emphasis added).

Lease production volumes and uniform quality likewise are, for purposes of royalty calculations, measured at the lease, not at off-lease treatment facilities. "Royalties shall be computed on the basis of the quantity and quality of

*unprocessed gas at the point of royalty settlement.*" 30 C.F.R. § 206.154(a)(1) (emphasis added). As the agency explained in adopting that rule:

> Historically, MMS has required that royalties be computed on the basis of the quantity and quality of unprocessed gas in marketable condition *as measured on the lease* * * * . This provision is consistent with the statutes, lease terms, and the gross proceeds valuation methodology because this provision establishes a point of royalty measurement upon which a quantity, *at a quality* is valued for royalty purposes.

53 Fed. Reg. 1230, 1255 (Jan. 15, 1988) (emphasis added).

The agency's unmistakable intent in those regulations is to calculate royalties based on the quantity and quality of the production as measured at the lease. Those regulations simply cannot support a valuation method under which royalties are based on the production's quality, after processing at a distant site, to meet the requirements for the "primary or dominant *end use* market." App., *infra*, 9a (emphasis added).

2. More fundamentally, neither the D.C. Circuit's decision nor the agency's explains how the two approaches to royalty calculation can textually co-exist. Either the MLA's reference to the value of "production * * * removed or sold from the lease" refers to the quality and quantity at the point of production or it does not. It cannot mean the quantity and quality removed or sold at the point of production for purposes of transportation expenses, work-back, and volume measurements, but quantity and quality measured at some entirely different point when it comes to determining marketable condition.

The D.C. Circuit thus erred by deferring to an agency interpretation that both contradicts the agency's express intent in adopting the regulations and construes the same text to have two different meanings at once. Deference to

an agency's interpretation of its regulations is inappropriate where an alternative interpretation is compelled by evidence of the agency's intent at the time of promulgation. *Thomas Jefferson Univ.* v. *Shalala*, 512 U.S. 504, 512 (1994) (citing *Gardebring v. Jenkins*, 485 U.S. 415, 430 (1988)). Moreover, deference to the agency's interpretation is only appropriate where the interpretation "sensibly conforms to the purpose and wording of the regulations." *Martin* v. *Occupational Safety and Health Review Comm'n*, 499 U.S. 144, 150-51 (1991) (quoting *Northern Indiana Pub. Serv. Co.* v. *Porter County Chapter of Izaak Walton League of America, Inc.* 423 U.S. 12, 15 (1975)). An agency cannot "rewrit[e] regulations under the guise of interpreting them." *Fina Oil and Chemical Co.* v. *Norton*, 332 F.3d 672, 676 (D.C. Cir. 2003). Nor can an agency rewrite or apply a single statutory phrase so as to have two diametrically opposed meanings in different contexts.

**D. The Issue Is Enormously Important**

Even apart from the other reasons for granting the petition, this case has enormous financial consequences. The United States has issued more than 26,000 leases for oil and gas deposits, and the annual royalties from those leases was more than $4.7 billion in 2004 alone. See Minerals Management Service, 2001-Forward MRM Statistical Information, http://www.mrm.mms.gov/MRMWebStats/Home.aspx; then follow the "Reported Royalty Revenues" hyperlink. The royalties for just the State of New Mexico that year were more than $500 million. *Ibid.*

The agency construction of the MLA affirmed in the decisions below will add hundreds of millions of dollars to those royalty obligations over the life of existing leases as the agency expands its new construction to other producers and contexts. Less than two weeks after the D.C. Circuit issued its decision in this case, the MMS issued another "Dear Payor" Letter requiring the significant costs of compressing natural gas, to prepare it for mainline trans-

portation, be added to the value of natural gas when calculating royalties—without regard for the fact that such compression typically is performed at third-party facilities. See U.S. Dep't of Interior, Minerals Management Service, Letter of Oct. 4, 2005, at 3-4. These staggering increases in royalty obligations should not be imposed absent this Court's review.

## II. The Courts Of Appeals Are Squarely Divided On Whether The Statute Of Limitations In 28 U.S.C. § 2415(a) Applies To Agency Orders Mandating The Payment Of Money

The decision below also holds that MMS orders assessing royalties are not limited by the statute of limitations codified at 28 U.S.C. § 2415(a). App., *infra*, 16a-20a. As the D.C. Circuit itself observed (App., *infra*, 18a), that holding squarely conflicts with the decisions of at least two other courts of appeals, including the Tenth Circuit's en banc decision in *OXY USA, Inc.* v. *Babbitt*, 268 F.3d 1001 (2001), and the Federal Circuit's decision in *United States* v. *Hanover Ins. Co.*, 82 F.3d 1052 (1996).

### A. The Ninth, Tenth, And Federal Circuits Have Held That Section 2415(a) Applies To Agency Proceedings To Recover For Breach Of Contract

Section 2415(a) provides, in relevant part:

> [*E*]*very action for money damages* brought by the United States * * * or agency thereof which is founded *upon any contract* * * * shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later.

28 U.S.C. § 2415(a) (emphasis added).

Court after court has concluded that Section 2415(a), by its terms, requires administrative actions seeking money

under a contract to be brought within six years. For example, the Tenth Circuit's decision in *OXY* applied Section 2415(a) to foreclose untimely MMS actions indistinguishable from the ones at issue here. In that case, the MMS issued an order in December of 1996 directing OXY USA, Inc. ("OXY") to pay additional royalties for oil production from federal leases in California for the period between January 1980 and September 1983. 268 F.3d at 1003-04. OXY challenged the MMS order, arguing that Section 2415(a) barred the MMS's belated demand. *Id.* at 1004. Sitting en banc, the Tenth Circuit rejected the government's contention that Section 2415(a) does not apply to administrative agency actions. Instead, the Tenth Circuit held that the MMS order is an action for money damages founded on a contract and that the six-year limitations period in Section 2415(a) therefore applies. *Ibid.*

Looking to the plain text of Section 2415, the Tenth Circuit observed that the phrase "every action" is "patently broad, and is expressly limited in scope only by reference to the possibility of a specific exception 'otherwise provided by Congress.'" *OXY*, 268 F.3d at 1005. The Tenth Circuit also pointed out that a broad reading of the phrase "every action" is consistent with the "express purpose of 28 U.S.C. § 2415(a)," which was "to establish a general statute of limitations on contract claims asserted by the government or a government agency." *Ibid.*

That conclusion is reinforced by the structure of Section 2415(a) as a whole. *OXY*, 268 F.3d at 1006. Under Subsection (f) of Section 2415, the federal government may assert claims defensively by way of an offset or counterclaim. *Ibid.* Subsection (i) expressly states that administrative offsets are exempt from the limitations period imposed by Section 2415(a). The Tenth Circuit reasoned that, if Congress believed that Section 2415(a) did not apply to administrative actions, then Congress would not have needed to carve out selected administration actions (admin-

istrative offsets) from Section 2415(a). 268 F.3d at 1006. It is, of course, wholly inappropriate to construe a statute so as to render any part of it superfluous.

The Tenth Circuit likewise held that the MMS order for additional royalties constituted an action for "money damages" within the meaning of Section 2415. The MMS order was based upon a contract, and the usual remedy for breach of contract is money damages. *OXY*, 268 F.3d at 1008. Moreover, the Tenth Circuit observed, the MMS order demanding additional royalties were indistinguishable from other government claims to recover money in which the limitations period in Section 2415(a) had been found to apply. *Ibid.*

In *Hanover*, 82 F.3d 1052, the Federal Circuit reached the same conclusion. That case concerned whether Section 2415(a) barred the Customs Service from seeking antidumping duties and interest in an agency enforcement action. Like the Tenth Circuit in *OXY*, the Federal Circuit concluded that Section 2415(a)'s six-year limitations period applies to administrative actions and is not limited to cases filed in court: An "[e]xamination of the language and the structure of section 2415(a) leaves the conviction that, absent an express exception, Congress intended that agencies assert their claims within six years or lose the right to enforce them." *Id.* at 1055.

The Ninth Circuit's decision in *United States* v. *Suntip Co.*, 82 F.3d 1468 (1996), is to the same effect. The question in *Suntip* was whether Section 2415(a) barred agency claims under the Contract Dispute Act for breach of federal timber sale contracts. Rejecting the contention that Section 2415(a)'s six-year limitations period is limited to actions in court, the Ninth Circuit held that the government must "submit that claim to a contracting officer within six years of accrual." *Id.* at 1476.

### B. The D.C. Circuit's Decision Conflicts With The Decisions Of The Ninth, Tenth, And Federal Circuits

In direct conflict with the Ninth, Tenth, and Federal Circuits, but consistent with an unpublished decision of the Fifth Circuit,[3] the D.C. Circuit's decision in this case held Section 2415(a) does not apply to agency proceedings seeking the payment of money. App., *infra*, 20a. The D.C. Circuit acknowledged that the Tenth and Federal Circuits had held that "subsection 2415(a) can apply to other administrative proceedings." *Id.* at 18a. But the D.C. Circuit rejected those courts' reasoning, holding that an MMS order for royalties is neither an action for "damages" nor a "complaint" within the meaning of Section 2415(a). Those terms, the D.C. Circuit ruled, refer exclusively to actions filed in court. *Id.* at 16a-17a. That construction cannot be reconciled with the decisions of the other courts of appeals, and the D.C. Circuit made no attempt at reconciliation. To the contrary, it acknowledged its disagreement with those decisions, and followed the reasoning of the dissenting opinions instead. *Id.* at 18a.

The D.C. Circuit's decision, moreover, is inconsistent with the ordinary understanding of statutory text. Courts often refer to actions for money owed under contract, whether before an agency or a court, as damages actions. See *OXY*, 268 F.3d at 1008; *United States* v. *Sackett*, 114 F.3d 1050, 1052 (10th Cir. 1997) (action to recover on defaulted Small Business Administration loans); *United States* v. *Alvarado*, 5 F.3d 1425, 1428 (11th Cir. 1993) (claim for damages on a promissory note). Congress likewise has used the term "complaint" and "damages" in connection with efforts to recover monetary compensation through administrative proceedings. See, *e.g.*, 15 U.S.C. § 45(b); 15

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[3] *Phillips Petroleum Co.* v. *Johnson*, No. 93-1377, 1994 WL 484506 (5th Cir. Sept. 7, 1994) ("Agency orders are * * * not barred by the limitations period of § 2415").

U.S.C. § 522; 25 U.S.C. § 2713; 29 U.S.C. § 160(b). There is no reason to believe Congress meant those words to have a narrower meaning here.

The D.C. Circuit's crabbed reading of Section 2415(a) is also at odds with the rule that statutes should be interpreted consonant with "the provisions of the whole law, and * * * its object and policy." See *John Hancock Mut. Life Ins. Co.* v. *Harris Trust and Sav. Bank*, 510 U.S. 86, 94-95 (1993); see also *FDA* v. *Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 133 (2000) ("A court must therefore interpret the statute 'as a symmetrical and coherent regulatory scheme,' *Gustafson* v. *Alloyd Co.*, 513 U.S. 561, 569 (1995), and 'fit, if possible, all parts into an harmonious whole,' *FTC* v. *Mandel Bros., Inc.*, 359 U.S. 385, 389 (1959)."). As the Tenth Circuit recognized in *OXY*, subsection (i) of Section 2415(a) states that *administrative offsets* are exempt from the limitations period imposed by Section 2415(a). *OXY*, 268 F.3d at 1006. That evidences Congress' intent that Section 2415(a) otherwise apply to administrative proceedings. By contrast, the D.C. Circuit's contrary construction renders Section 2415(i)'s exception for administrative offsets wholly superfluous, as the D.C. Circuit itself conceded, App. *infra*, 18a. If the limitations period does not apply to any administrative proceedings in the first instance, the exception for offsets in administrative proceedings would serve no function at all. The D.C. Circuit's narrow reading of "damages" and "complaint" is also inconsistent with the overall objective behind Section 2415(a), which was to provide a broad, catch-all limitations period. *OXY*, 268 F.3d at 1005.

The D.C. Circuit attempted to reconcile the import of subsection (i) with its narrow interpretation of Section 2415(a) by referring to legislative history that, in its view, showed that subsection (i) was a compromise between the Comptroller General and the Justice Department. App., *infra*, 18-19a. Putting aside the legislative history indi-

cating that Congress intended Section 2415(a) to limit actions before courts and agencies alike,[4] the D.C. Circuit's attempt to utilize legislative history to alter the plain import of subsection (i) is contrary to settled principles of statutory construction. See *Ratzlaf* v. *United States*, 510 U.S. 135, 147 (1994) ("There are, we recognize, contrary indications in the statute's legislative history. But we do not resort to legislative history to cloud a statutory text that is clear") (footnote omitted); *Missouri Pac. R. Co.* v. *United States*, 278 U.S. 269, 278 (1929) (holding that, where statutory text is clear, "legislative history may not be used to support a construction that adds to or takes from the significance of the words employed.")

### C. The Conflict Concerning The Meaning Of Section 2415(a) Is Of Recurring Importance In Many Contexts.

As the D.C. Circuit observed, Congress has since amended the Mineral Leasing Act to provide a specific limitations period for MMS demands for money under that statute. See App., *infra*, 16a.[5] But whether Section 2415(a) applies to agency proceedings remains an issue of recurring and increasing importance in many contexts.

Both the Federal Circuit and the Ninth Circuit decisions holding Section 2415(a) applicable to administrative proceedings arose outside the Mineral Leasing Act context. In *Hanover*, *supra*, for example, the Federal Circuit held that

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[4] See *Phillips Petroleum Co.* v. *Lujan*, 4 F.3d 858, 863 (10th Cir. 1993) ("The legislative history in support of § 2415(a) indicates Congress was motivated in part by notions of fairness and equity in government dealings with private litigants, and further motivated to reduce the costs of record keeping and encourage *prompt agency* actions on claims.") (emphasis added).

[5] Congress established an across-the-board seven-year statute of limitations for production after September 1, 1996. See Federal Oil and Gas Royalty Simplification and Fairness Act of 1996, Pub. L. No. 104-185, 110 Stat. 1700 (codified at 30 U.S.C. § 1724).

Section 2415(a) barred the Customs Service from seeking antidumping duties and interest, even though Customs sought the duties in an agency enforcement action. An "[e]xamination of the language and structure of Section 2415," the Federal Circuit held, "leaves the conviction that, absent an express exception, Congress intended that agencies assert their claims within six years or lose the right to enforce them." *Hanover*, 82 F.3d at 1055. Similarly, in *Suntip*, *supra*, the Ninth Circuit applied Section 2415(a) to bar untimely agency action under the Contract Dispute Act in connection with an alleged breach of federal timber sale contracts. Explaining the limitations that Section 2415(a) places on government claims, the Ninth Circuit stated that the government must "submit [its] claim to a contracting officer within six years of accrual." *Suntip*, 82 F.3d at 1476.

The *Hanover* and *Suntip* decisions both demonstrate that whether the limitations period found in Section 2415(a) applies both to administrative and judicial proceedings, or solely to judicial proceedings, is a question that arises in many contexts other than oil and gas leases. Indeed, the issue can arise under any of the many statutory schemes in which an agency may initiate proceedings to recover money under an agreement. The timeliness of government actions for money ought not depend on the happenstance of the court of appeals in which agency proceedings are enforced or reviewed. This Court should grant the petition and resolve the square and irreconcilable conflict among the courts of appeals.

## CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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NOVEMBER 2005

## APPENDIX A

## UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

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AMOCO PRODUCTION COMPANY,
*APPELLANT*

v.

REBECCA W. WATSON, ASSISTANT SECRETARY FOR LAND AND MINERAL MANAGEMENT, ET AL.,
*APPELLEES*

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Nos. 04-5006, 04-5007.

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Argued Feb. 14, 2005.
Decided June 10, 2005.

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Before: EDWARDS, SENTELLE, and ROBERTS, *Circuit Judges*.

Opinion for the Court filed by *Circuit Judge* ROBERTS.

ROBERTS, *Circuit Judge*: The San Juan Basin covers 7500 square miles in northwest New Mexico and southwest Colorado. Since the end of World War II, it has been a prolific source of natural gas, connected by pipeline to southern California and literally helping to fuel the dramatic growth of that region. Beginning in the 1980s, large-scale extraction of the variety of natural gas known as coalbed methane began to supplement the supply of conventional gas from the region. Coalbed methane contains upwards of ten percent carbon dioxide, which is largely absent from conventional natural gas. Because carbon dioxide does not produce energy, mainline natural

gas pipelines will not accept gas with a carbon dioxide component of more than two to three percent of volume. A high carbon dioxide content does not render the natural gas useless for consumers, but if producers in the San Juan Basin want to sell their gas to markets beyond that sparsely populated region, they must use the mainline and meet its more stringent carbon dioxide standard.

The federal government is a large landowner in the San Juan Basin and, like many other owners of property rich in natural gas, it leases rights to extract the gas in exchange for a percentage of the proceeds. Unlike the case with other landowners, however, the relationship between the government and those who extract gas from the government's land is regulated pursuant to an elaborate array of statutes and rules. The present case involves several disputes between the government and gas producers over how the need to remove the excess carbon dioxide from coalbed methane, to make it palatable to the mainline pipelines, affects the royalty payment the producers owe the government under those statutes and regulations. For the reasons that follow, we affirm the district court's decision and uphold the government's determination that the producers owe additional royalties.

## I. Background

*Statutory and Regulatory Framework.* The Department of the Interior (DOI), through its Minerals Management Service (MMS), issues and administers leases authorizing the extraction of natural gas from government land. The Mineral Leasing Act (MLA), 30 U.S.C. §§ 181 *et seq.* (2000), requires producer-lessees to pay the government-lessor "a royalty at a rate of not less than 12.5 percent in amount or value of the production removed or sold from the lease." *Id.* § 226(b)(1)(a). To ensure the government gets its due in royalties, the Secretary of the Interior is directed by statute to establish a comprehensive inspection, auditing, and collection system. *See id.* § 1711.

In 1988, pursuant to these statutes, MMS "amended and clarified" the rules "governing valuation of gas for royalty computation purposes." Revision of Gas Royalty Valuation Regulations and Related Topics, 53 Fed.Reg. 1230 (Jan. 15, 1988). Under these new regulations, MMS specified that the "value of the production" referred to in 30 U.S.C. § 226(b)(1)(A) must be no less than "the gross proceeds accruing to the lessee for lease production," minus certain allowable deductions. 30 C.F.R. § 206.152(h) (1988). A factor in calculating these "gross proceeds" is a longstanding interpretation of the MLA that obligates lessees to put the gas they extract in "marketable condition at no cost to" the federal lessor. *Id.* § 206.152(i); *see California Co. v. Udall*, 296 F.2d 384, 387-88 (D.C. Cir. 1961) (upholding marketable condition requirement). Under the 1988 regulations, lease products are considered in marketable condition if they "are sufficiently free from impurities and otherwise in a condition that they will be accepted by a purchaser under a sales contract typical for the field or area." 30 C.F.R. § 206.151. If a lessee sells "unmarketable" gas at a lower cost, the gross proceeds for purposes of royalty calculation must be "increased to the extent that gross proceeds have been reduced because the purchaser, or any other person, is providing certain services" to place the gas in marketable condition. *Id.* § 206.152(i). To take a simple example, if it costs $20 to put gas in marketable condition by removing impurities, and the purified gas is sold for $100, "gross proceeds" for purposes of royalty calculations is $100, regardless of whether the producer removes the impurities and sells the gas for $100, or instead sells the gas for $80 to a purchaser who then removes the impurities.

The regulations allow lessees to deduct from gross proceeds costs directly related to transporting gas from the wellhead for sale at markets remote from the lease. *See id.* § 206.157(a)-(b). The government's generosity with respect to this deduction, however, goes only so far—absent

approval from MMS, a lessee is not allowed to deduct the costs of transporting non-royalty bearing products. *See id.* § 206.157(a)(2)(i), (b)(3)(i). In other words, to the extent the government is not going to share in the proceeds of the producers' distant sale, because some of the product is non-royalty bearing, the government does not in effect share in the cost of transporting that portion of the product by having that cost deducted from "gross proceeds." There is an exception to this logic: a portion of the product may fall into a category known as "waste products which have no value." *Id.* § 206.157(a)(2)(i), (b)(3)(i). Although it may at first seem counterintuitive, the government allows a deduction for the cost of transporting such waste products, because such transport is considered part of the cost of transporting the royalty-bearing product with which the waste products are associated.

*Facts and Rulings Below.* Producers Amoco Production Company (Amoco) and Atlantic Richfield Company and Vastar Resources, Inc. (ARCO/Vastar) produce coalbed methane on public land in the San Juan Basin pursuant to leases with the federal government. To make the coalbed methane suitable for transportation over mainline pipelines, the producers arranged for the removal of excess carbon dioxide from most of the gas they extracted. Between 1989 and 1996, the producers sold untreated gas at the wellhead to purchasers who would pipe the gas to treatment centers, remove the excess carbon dioxide, and then put the treated gas on the mainline system for transport and sale to end-users throughout the country. The producers' sales arrangements differed; Amoco would sell untreated gas primarily to a wholly-owned trading subsidiary and ARCO/Vastar would contract arms-length sales with unaffiliated purchasers. Nevertheless, the economics of the transactions were the same, with the price of untreated gas at the wellhead reflecting the fact that the purchaser would have to transport the gas to treatment plants and remove the

excess carbon dioxide before sending the gas into the mainline.

On April 22, 1996, MMS issued a letter to lease operators and royalty payors in the San Juan Basin laying out the Service's "guidelines" for calculating royalties on coalbed methane. Payor Letter, at 1. The Payor Letter informed the producers that removing excess carbon dioxide was considered a cost of placing the gas in marketable condition. Consequently, producers who removed the gas themselves could not deduct the cost of doing so from gross proceeds, and those selling untreated gas at a lower price nevertheless needed to add back to gross proceeds the cost of removal services performed by the purchaser. *See id.* at 1-2. The letter also addressed transportation allowances, specifying that producers could deduct the costs of piping the methane and the allowable two to three percent portion of carbon dioxide to the treatment center, but not the cost of transporting the excess carbon dioxide to be removed at the center. In the government's view, that excess constituted a non-royalty bearing product under the regulations. *See id.* at 2-3.

On the heels of the Payor Letter, MMS issued separate orders finding Amoco and ARCO/Vastar deficient in their royalty payments for the period between 1989 and 1996. This shortfall stemmed from the producers' accounting for sales of raw coalbed methane that was later treated and marketed on the mainline by its purchasers. In calculating gross proceeds, the producers did not add back the costs incurred by the purchasers in moving the excess carbon dioxide to the treatment plant and removing it once there. Instead, they calculated gross proceeds the same way they did for sales of coalbed methane used in untreated form by local purchasers. MMS thus concluded that Amoco and ARCO/Vastar owed the government additional royalties totaling $4,117,607 and $782,373, respectively. The producers did not have to add back to gross proceeds the cost of trans-

porting royalty-bearing methane and the allowable three percent carbon dioxide "waste product"—because this cost was deductible in the government's view—and the orders did not assess any additional royalties on sales of gas consumed without treatment.

In separate challenges to these orders before the Assistant Secretary for Land and Minerals Management, the producers argued that untreated gas at the wellhead was already in marketable condition—after all, they sold a fair amount of it in that form, and it was used without treatment—so there was no reason to augment their gross proceeds for royalty calculation purposes. They also argued that the cost of piping the excess carbon dioxide to the treatment plant should be viewed as a deductible transportation cost, not a cost of putting the gas in marketable condition. In the alternative, the producers contended that, under the transportation regulations, the excess carbon dioxide piped to the treatment plants should be regarded as a "waste product." The Assistant Secretary rejected these challenges and also concluded—contrary to the producers' contentions—that the Payor Letter was not a rule, and so was not subject to the Administrative Procedure Act's notice and comment requirement. *See* 5 U.S.C. § 553. The Assistant Secretary also rejected the producers' argument that collection of the royalties was barred by the six-year statute of limitations for government actions for money damages found in 28 U.S.C. § 2415.

In the District Court for the District of Columbia, the producers sought a declaratory judgment and injunction against enforcement of the MMS orders. On cross-motions for summary judgment, the district court ruled for the government. *See Amoco Production Co. v. Baca*, 300 F. Supp. 2d 1 (D.D.C.2003). Amoco and ARCO/Vastar appeal.

## II.

We review the district court decision *de novo*, *Fina Oil & Chem. Co. v. Norton*, 332 F.3d 672, 675-76 (D.C. Cir. 2003), and will reverse the Assistant Secretary's rulings only if they are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law," or if they are "in excess of statutory jurisdiction, authority, or limitations, or short of statutory right." 5 U.S.C. § 706(2)(A), (C); *Gerber v. Norton*, 294 F.3d 173, 178 (D.C. Cir. 2002).

**A.** We first turn to the producers' argument that the Assistant Secretary's application of the marketable condition rule violates the MLA. The Assistant Secretary concluded that "the value for royalty purposes must be determined by adding to the gross proceeds received from the wellhead purchaser the cost of treating the gas . . . to the level required to place the gas in marketable condition." MMS Decision of Sept. 12, 2000 (Amoco Decision) at 10 [J.A. 11]; MMS Decision of Mar. 24, 2000 (ARCO/Vastar Decision) at 6. The producers contend this conclusion cannot be squared with the statutory provision requiring producers to pay royalties based on the "amount or value of the production removed or sold *from the lease*." 30 U.S.C. § 226(b)(1)(A) (emphasis added). The producers read the underscored phrase as requiring that the physical leasehold be treated as the relevant geographic market, precluding calculation of royalties based on gross proceeds derived from sales remote from the wellhead.

We review the agency's interpretation of the MLA, a statute DOI administers, within the framework of *Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837, 104 S.Ct. 2778, 81 L. Ed. 2d 694 (1984). *See Indep. Petroleum Ass'n of Am. v. DeWitt*, 279 F.3d 1036, 1039-40 (D.C. Cir. 2002) ("*IPAA*"). Under the first step of *Chevron*, we inquire whether Congress has spoken directly to the question at issue. 487 U.S. at 842, 108 S.Ct. 2687. If so, we give effect to that clearly expressed intent. If instead the

statute is "silent or ambiguous with respect to the specific issue," we defer to the agency interpretation, so long as it is reasonable. *Id.* at 842-43, 108 S.Ct. 2687.

Although the producers present a textually plausible reading of section 226, theirs is not the only one available. The phrase "from the lease" is sufficiently broad to be read as referring simply to the origin of the gas. Gas that is "from the lease" and that is marketed at a remote location can readily be described as gas "removed or sold from the lease." The producers read the statute as if it referred to gas "sold *at* the lease," but that is not the case. They direct us to no precedent limiting marketable condition to their narrowing construction. Although they observe that this court in *California Co.* applied the marketable condition rule to sales of treated gas near the wellhead, that is of little help to them; *all* the gas at issue there "was conditioned by the seller and delivered to the purchaser within a short distance of the wells," 296 F.2d at 387, so the question presented here did not arise.

The producers' reliance on our more recent decision in *IPAA* is also misplaced. They direct to us to a portion of the opinion observing that DOI "abide[s] by the statutory mandate to base royalty on the 'value of the production removed or sold from the lease,'" 279 F.3d at 1037 (quoting 30 U.S.C. § 226(b)(1)(A)), but the cited dictum does not even interpret "from the lease," let alone do so authoritatively. If anything, *IPAA* was skeptical of the producers' "almost metaphysical" proposition "that the sale of 'marketable condition' gas at the leasehold represent[ed] a baseline" beyond which the government had to share any costs incurred further down the line. *Id.* at 1041.

Because the Assistant Secretary has not interpreted the statute in a manner contrary to clear congressional intent, the next step is to ask whether her construction is a reasonable one. *See Chevron*, 467 U.S. at 843, 104 S.Ct. 2778. The producers do not, however, appear to marshal a step two ar-

gument. Consequently, we have no basis for finding the Assistant Secretary's interpretation unreasonable. *See Consumer Elec. Ass'n v. FCC*, 347 F.3d 291, 299 (D.C. Cir. 2003).

**B.** The producers also contend that the Assistant Secretary acted arbitrarily and capriciously by misinterpreting the MLA regulations and departing from agency precedent. Although we will not allow an agency to "rewrit[e] regulations under the guise of interpreting them," *Fina Oil*, 332 F.3d at 676, we nevertheless owe "substantial deference to an agency's interpretation of its own regulations," giving that interpretation "controlling weight unless it is plainly erroneous or inconsistent with the regulation," *Thomas Jefferson Univ. v. Shalala*, 512 U.S. 504, 512, 114 S.Ct. 2381, 129 L. Ed. 2d 405 (1994) (internal quotation marks omitted). Such deference is particularly appropriate in the context of "'a complex and highly technical regulatory program,' in which the identification and classification of relevant 'criteria necessarily require significant expertise and entail the exercise of judgment grounded in policy concerns.'" *Id.* (quoting *Pauley v. BethEnergy Mines, Inc.*, 501 U.S. 680, 697, 111 S.Ct. 2524, 115 L. Ed. 2d 604 (1991)).

The producers argue that the DOI regulation defining gas in "marketable condition" as gas acceptable to "a purchaser under a sales contract typical for the field or area," 30 C.F.R. § 206.151, requires MMS to consider untreated gas sold at the wellhead to be in marketable condition, notwithstanding any later off-lease treatment. The Assistant Secretary concluded, however, that because the "dominant market for gas from the area is for gas that is utilized in distant markets with a much lower $CO_2$ content," sales contracts for *treated* gas were typical for the area, while those for untreated gas were not. Amoco Decision at 7; *see also* ARCO/Vastar Decision at 5. Although the producers concede that most of the gas purchased at their leaseholds is treated for use in downstream markets, they argue that

the Assistant Secretary's "dominant end-use" rationale is irreconcilable with the text of section 206.151 of the regulations, which frames typicality in terms of a given "field or area."

We are not persuaded, however, that the regulations require MMS to understand typical sales contracts—and thus marketable condition—as relating to transactions at the leasehold or immediately nearby. As an initial matter, it is not even clear that "field or area"—the textual hook for the producers' interpretation—refers only to leasehold land. The regulations define "area" as "a geographic region *at least as large* as the defined limits of [a] gas field, in which . . . gas lease products have similar quality, economic, and legal characteristics," and define "field" as "a geographic region situated over one or more subsurface . . . gas reservoirs encompassing *at least* the outer-most boundaries of all . . . gas accumulations." 30 C.F.R. § 206.151 (emphases added). Because these terms do not foreclose the possibility of defining a region beyond the geographical limits of a leasehold, we are hesitant to conclude that the Assistant Secretary's interpretation failed to "sensibly conform[ ] to the purpose and wording of the regulations." *Martin v. Occupational Safety and Health Review Comm'n*, 499 U.S. 144, 151, 111 S.Ct. 1171, 113 L. Ed. 2d 117 (1991) (internal quotation marks omitted).

The producers' construction also does not square with the regulatory scheme as a whole. The regulation stipulating that producers are to place gas in marketable condition at no cost to the government does not contain a geographic limit. *See* 30 C.F.R. § 206.152(i). More importantly, regulations governing transportation allowances obviously assume that valuation of gas "at a point (e.g., sales point or point of value determination) off the lease" is permissible. *Id.* § 206.156(a). The Assistant Secretary's approach to the marketable condition rule is entirely consistent with this regulatory scheme and the basic principle that the MLA

contemplates a meaningful distinction between marketing and merely selling gas. *See California Co.*, 296 F.2d at 388.

The Assistant Secretary's approach to marketable condition should not have surprised the producers. When soliciting comments for the 1988 rulemaking that led to reiteration of the marketable condition rule in regulation 206.152, the agency entertained suggestions from producers that the government lessor should share treatment costs, by allowing producers to deduct all post-production costs under the theory that royalties are "due on the market value of production at the lease or well." 53 Fed.Reg. at 1252. Otherwise, industry commentators argued, MMS would "improperly sweep[ ] all post-production operations under the holding of [*California Co.*]." *Id.* MMS considered but rejected this suggestion, concluding that "so-called post-production costs . . . [g]enerally . . . are not allowed as a deduction because they are necessary to make production marketable." *Id.* at 1253.

The producers alternatively contend that, because there is an established demand for untreated gas, sales of such gas at the wellhead should be treated as "typical" for defining marketable condition. It is true that fifteen to twenty percent of the gas purchased from the producers was consumed locally, and it is plausible to conclude that contracts for one-fifth of a product are common enough to be "typical." But it is just as plausible to read typicality as embracing the *most* common use and sale of gas from the area, and it is not at all obvious from the text and purposes of the regulations that contracts for one-fifth of the gas should govern the regulatory treatment of the remaining eighty percent.

Finally, we disagree with the producers' argument that the Assistant Secretary impermissibly departed from agency precedent. In *Xeno, Inc.*, the agency concluded gas was in marketable condition at the wellhead based on evidence of competing purchase offers there. 134 I.B.L.A. 172,

180-84 (1975). Central to *Xeno*, however, was the fact that the gas was suitable for pipeline access *before* gathering and compression, a quality reflected in its price at the wellhead. *See id.; see also Amerada Hess Corp. v. Dep't of Interior*, 170 F.3d 1032, 1037 (10th Cir. 1999) (distinguishing Xeno when a producer had not shown gas was in marketable condition at the wellhead).

Nor is *Beartooth Oil & Gas Co. v. Lujan*, No. 92-99 (D. Mont. Sept. 22, 1993), to the contrary. *Beartooth* overruled a decision that, in assessing royalties on wellhead sales, included the value of subsequent compression and delivery by a purchaser. Even if this unpublished district court opinion—withdrawn after a settlement—bound MMS, it is readily distinguishable. The *Beartooth* court ruled for the producer not because the court was certain the gas was in marketable condition at the wellhead, but rather because the agency did not make findings supporting the assertion that the gas was not. *See Beartooth* at 9-10. Here, the Assistant Secretary explained in detail why the gas was not in marketable condition at the wellhead. *See* Amoco Decision at 9-11; ARCO/Vastar Decision at 6-7.

**III.**

The Assistant Secretary allowed the producers to deduct from gross proceeds the costs of transporting the royalty-bearing methane and the three percent carbon dioxide "waste product" to the treatment plant, but not the costs of transporting and removing the excess carbon dioxide. The producers argue that some or all of the costs of ridding the gas of excess carbon dioxide should be deductible from gross proceeds as a cost of transporting the gas to market under 30 C.F.R. § 206.157(a)-(b).

To argue that all the extra costs are deductible, the producers liken these expenses to "firm demand" charges—nonrefundable deposit payments required to reserve pipeline capacity. DOI argued that such charges were not rela-

ted to transportation in *IPAA*, but we did not accept DOI's argument. *See* 279 F.3d at 1042 ("While some reason may lurk behind the government's position, it has offered none, and we have no basis for sustaining its conclusion."). The producers contend that, like firm demand charges, the costs at issue here are necessary to secure access to a mainline system that will not accept gas with a carbon dioxide content of more than two or three percent. In support of their argument, they also cite two other cases purportedly regarding pre-pipeline treatment as a transportation cost: *Exxon Corp.*, 118 I.B.L.A. 221 (1991) and *Marathon Oil Co. v. United States*, 604 F. Supp. 1375 (D. Alaska 1985).

Unlike the case in *IPAA*, however, here the Assistant Secretary has explained why the costs at issue are not properly considered transportation costs: because removal of the excess carbon dioxide was necessary to place the gas in marketable condition, those same costs could not be part of the transportation allowance. The logic of the regulations bars an expenditure to place gas in marketable condition from also being an expenditure deductible from gross proceeds as a transportation cost. *See* 30 C.F.R. § 206.152(i) (lessees must "place gas in marketable condition at no cost to the Federal Government"). Because we uphold the Assistant Secretary's conclusion that these costs are necessary to place the gas in marketable condition, we cannot quarrel with her rejection of the producers' transportation theory. Unsurprisingly, none of the cases the producers cite deals with deducting costs necessary for placing gas in marketable condition. The firm demand charges to reserve space on the pipeline at issue in *IPAA*, for example, related solely to transportation and had nothing to do with conditioning the gas for market. *See IPAA*, 279 F.3d at 1042; *see also Marathon Oil*, 604 F. Supp. at 1386 (costs of liquefying natural gas deductible because done "for purposes of storage or shipment" and end-product "chemically identical to the natural gas at the lease"); *Exxon Co.*, 118 I.B.L.A. at

242 (deductible dehydration of gas "was not performed to satisfy market specifications").

Seeking at least half a loaf, the producers argue the Assistant Secretary erred in treating the excess carbon dioxide (the amount beyond the pipeline threshold) as a non-royalty-bearing product, whose transportation cost is nondeductible. The producers contend that the carbon dioxide in excess of the pipeline tolerance should have been treated the same as that within the tolerance—as a waste product—with the result that the deductible transportation cost would not be reduced by the cost of transporting any of the carbon dioxide.

Although carbon dioxide is carbon dioxide, there is a meaningful distinction in the regulation between the amount that may be marketed along with the gas, and the excess that must be removed to make the gas marketable. The two *amounts* need not be treated the same under the rules, simply because they are the same *product*. Within the pipeline tolerance, carbon dioxide is a waste product because it need not be removed to place the gas in marketable condition; beyond the tolerance, the carbon dioxide is a non-royalty-bearing product that must be removed for the gas to considered marketable under the rules. This difference has the consequence ascribed by the Secretary when it comes to determining the deductibility of transportation costs.

The producers rely on an illustrative example in the MMS-issued Payor Handbook that treats carbon dioxide in a manner suggesting it is waste. This example—which does not purport to be a rule and concerns a carbon dioxide content of only one percent, *see* 3 MINERALS MGMT. SERV., U.S. DEP'T OF THE INTERIOR, OIL & GAS PAYOR HANDBOOK § 6.4.1 (1993)—hardly compels the agency to treat a ten percent component of carbon dioxide as waste, let alone creates an inference that carbon dioxide is always waste.

## IV.

The producers also challenge the Payor Letter cited in the orders and in the Assistant Secretary's decisions, arguing that it constituted a new rule the agency could promulgate only through notice and comment rulemaking. *See* 5 U.S.C. § 551(4) (defining a rule as "the whole or part of an agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy or describing the organization, procedure or practice requirements of an agency"). Rejecting the Assistant Secretary's explanation that the Payor Letter was merely an interpretation of existing regulations, the producers ask us to set it aside and consider the Assistant Secretary's reliance upon it unlawful because the agency did not promulgate the rule as required by the Administrative Procedure Act. *See id.* § 553(b)(3)(A).

This challenge is governed by *Indep. Petroleum Ass'n of Am. v. Babbitt*, which held that a similar MMS letter was not a rule subject to the notice and comment requirement. 92 F.3d 1248, 1256-57 (D.C. Cir. 1996). As in *Babbitt*, the Payor Letter here is not an agency statement with future effect because nothing under DOI regulations vests the Letter's author—in *Babbitt* and this case MMS's Associate Director for Royalty Management—with the authority to announce rules binding on DOI. *Id.* at 1256. "The letter is not an agency rule at all, legislative *or* otherwise, because it does not purport to, nor is it capable of, binding the agency." *Id.* at 1257.

The producers attempt to distinguish *Babbitt* by alleging that here the agency adopted the Payor Letter's positions when it issued and affirmed the orders. But nothing in the decisions under review suggests that the agency viewed the Payor Letter as authoritative or binding; the agency in those decisions applied the pertinent statutes and regulations with no determinative reliance on the Payor Letter. The agency decisions reached the same result as the gui-

dance in the Payor Letter, but that was true in *Babbitt* as well. The sort of "workaday advice letter[s] that agencies prepare countless times per year in dealing with the regulated community," *Indep. Equip. Dealers Ass'n v. EPA*, 372 F.3d 420, 427 (D.C. Cir. 2004) (internal quotation marks omitted), do not retroactively become agency rules whenever they are referenced in an agency decision.

V.

Finally, the producers argue that the district court and the Assistant Secretary erred in concluding that the MMS orders assessing additional royalties were not barred by the statute of limitations found at 28 U.S.C. § 2415(a).[1] That provision specifies that

> [E]very action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later.

The threshold question is whether an administrative order assessing additional royalties can reasonably be understood to be an "action for money damages" initiated by the filing of a "complaint." The phrase "action for money damages" points strongly to a suit in a court of law, rather than an agency enforcement order that happens to concern money due under a statutory scheme. *See* BLACK'S LAW DIC-

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[1] The dispute about the applicability of 28 U.S.C. § 2415(a) to demands for additional royalties is no longer a live one with respect to production after September 1, 1996, for which Congress has set a seven-year limitations period. *See* Federal Oil and Gas Royalty Simplification and Fairness Act of 1996, Pub.L. No. 104-185, 110 Stat. 1700 (codified at 30 U.S.C. § 1724).

TIONARY 389 (6th ed. 1990) (defining "damages" as "pecuniary compensation or indemnity, which may be recovered in the courts"); *OXY USA, Inc. v. Babbitt*, 268 F.3d 1001, 1010 (10th Cir. 2001) (en banc) (Briscoe, J., dissenting) ("Taken together, the entire phrase plainly and indisputably refers to lawsuits brought by the federal government seeking compensatory relief for losses suffered by the government.").

Any doubt is removed by the fact that subsection 2415(a) measures the limitations period from the filing of a "complaint." It strains legal language to construe this administrative compliance order as a "complaint" for money damages in any ordinary sense of the term. *See* BLACK'S LAW DICTIONARY 285 (6th ed. 1990) (defining complaint as an "initial pleading" under "codes or Rules of Civil Procedure" that contains, *inter alia*, a "statement of the grounds upon which the *court's* jurisdiction depends") (emphasis added). Although some statutes provide for a "complaint" that triggers administrative proceedings, *see, e.g.*, 5 U.S.C. § 1215(a)(1); 15 U.S.C. §§ 45(b), 522; 25 U.S.C. § 2713(a)(3); 29 U.S.C. § 160(b), adjudicative hearings on the merits follow such filings. Here MMS issued an *order*, the defiance of which incurs a "Notice of Noncompliance" and subsequent civil penalties, absent a successful appeal. *See* 30 C.F.R. § 241.51 (1996); *see also* BLACK'S LAW DICTIONARY 1096 (6th ed. 1990) (defining order as "[a] mandate; precept; command or direction authoritatively given; rule or regulation").

While we are satisfied from the text of subsection 2415(a) that the agency action at issue here does not fall under the clause's purview, the statute as a whole is admittedly less clear. One of the statute's enumerated exceptions—added more than 16 years after the passage of the original Act, *see* Debt Collection Act of 1982, Pub.L. No. 97-365, § 9, 96 Stat. 1749, 1754—states that "[t]he provisions of this section shall not prevent the United States or an officer or agency thereof from collecting any claim of the United States by

means of administrative offset, in accordance with section 3716 of title 31." 28 U.S.C. § 2415(i). The producers contend that subsection 2415(a) must apply to administrative proceedings generally, or there would have been no need to except administrative offsets in subsection (i).

This argument is not without force. It is a familiar canon of statutory construction that, "if possible," we are to construe a statute so as to give effect to "every clause and word," *United States v. Menasche*, 348 U.S. 528, 538-39, 75 S.Ct. 513, 99 L.Ed. 615 (1955) (internal quotation marks omitted), and the producers' argument has helped convince two other circuits that subsection 2415(a) can apply to other administrative proceedings, *see OXY USA*, 268 F.3d at 1006; *United States v. Hanover Ins. Co.*, 82 F.3d 1052, 1055 (Fed. Cir. 1996). In this case, however, the inference to be drawn from the addition of subsection 2415(i) does not dissuade us from the more natural reading of the express language of subsection 2415(a). As the Supreme Court recently explained, "our preference for avoiding surplusage constructions is not absolute." *Lamie v. U.S. Trustee*, 540 U.S. 526, 124 S.Ct. 1023, 1031, 157 L. Ed. 2d 1024 (2004). *See Chickasaw Nation v. United States*, 534 U.S. 84, 89, 122 S.Ct. 528, 151 L. Ed. 2d 474 (2001) (adopting construction that leads to surplusage because "we can find no other reasonable reading of the statute"). No canon of construction justifies construing the actual statutory language beyond what the terms can reasonably bear. *See Conn. Nat'l Bank v. Germain*, 503 U.S. 249, 252-53, 112 S.Ct. 1146, 117 L. Ed. 2d 391 (1992).

The context surrounding the passage of subsection 2415(i) gives us some comfort that the provision is not so much surplusage as the result of a congressional effort to moot a debate between the Justice Department and the Comptroller General about the reach of subsection 2415(a) in the context of administrative offsets. The Justice Department thought subsection 2415(a) might be invoked to

bar administrative offsets; the Comptroller General concluded that it was not applicable in that context. The Comptroller General nevertheless recommended that Congress enact subsection 2415(i) "as a means of resolving the differences between us." *Debt Collection Act of 1981: Hearings on S.1249 before the Senate Commitiee on Governmental Affairs*, 97th Cong. 83 (1981) (statement of Milton J. Socolar, Acting Comptroller General). "By adopting section 2415(i), Congress thus did not have to decide whether the Department of Justice or the Comptroller General had the better of the argument as to the proper construction of the pre-1982 version of section 2415." *Hanover Ins. Co.*, 82 F.3d at 1057 (Bryson, J., dissenting). We think it clear that subsection 2415(a), by its terms, does not cover administrative actions, and the fact that Congress "sought to make [the] statute crystal clear rather than just clear" in the context of administrative offsets does not alter our conclusion. *In re Collins*, 170 F.3d 512, 513 (5th Cir. 1999).

Finally, buttressing our conclusion not to let subsection 2415(i) alter the clear import of 2415(a) is the opposing canon (there always seems to be one) that statutes of limitations against the sovereign are to be strictly construed. *See E.I. du Pont de Nemours & Co. v. Davis*, 264 U.S. 456, 462, 44 S.Ct. 364, 68 L.Ed. 788 (1924); *Hanover Ins. Co.*, 82 F.3d at 1057 (Bryson, J., dissenting). Expanding the apparent scope of a statute of limitations beyond its plain language by inference from an express exception is hardly strict construction. Similar concerns helped dissuade the Supreme Court from relying on the surplusage canon in *Chickasaw Nation*. *See* 534 U.S. at 90, 122 S.Ct. 528 (application of surplusage canon would contravene rule that Congress ordinarily enacts tax exemptions explicitly).

Although other courts addressing this question have emphasized the underlying purpose of repose animating section 2415, *see OXY USA*, 268 F.3d at 1005-06; *Hanover Ins. Co.*, 82 F.3d at 1055, the Supreme Court has frequently

warned that such appeals to purpose cannot override a statute's clear language, *see, e.g., Badaracco v. Comm'r of Internal Revenue*, 464 U.S. 386, 398, 104 S.Ct. 756, 78 L. Ed. 2d 549 (1984) ("Courts are not authorized to rewrite a statute because they might deem its effects susceptible of improvement. This is especially so when courts construe a statute of limitations, which must receive a strict construction in favor of the Government.") (internal quotation marks and citation omitted). Consequently, we join the Fifth Circuit, *see Phillips Petroleum Co. v. Johnson*, No. 93-1377, 1994 WL 484506 (5th Cir. Sept 7, 1994), in concluding that the statute of limitations in subsection 2415(a) does not apply to bar an administrative order demanding payment owed pursuant to the MLA and its regulations.

Because we conclude that the government's demand for additional royalties is not an action for money damages initiated by the filing of a complaint, we do not need to address the government's further arguments that the demand neither seeks "money damages" nor is "founded upon a contract." 28 U.S.C. § 2415(a).

The judgment of the district court is

*Affirmed.*

## APPENDIX B

## UNITED STATES DISTRICT COURT, DISTRICT OF COLUMBIA

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AMOCO PRODUCTION COMPANY,
*PLAINTIFF,*

v.

SYLVIA V. BACA, ET AL.,
*DEFENDANTS.*

VASTAR RESOURCES, INC. AND ATLANTIC RICHFIELD COMPANY,
*PLAINTIFFS,*

v.

SYLVIA V. BACA, ET AL.,
*DEFENDANTS.*

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Nos. CIV.A. 00-02933 (WBB),
CIV.A. 00-01480 (WBB)

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Nov. 14, 2003.

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## MEMORANDUM

BRYANT, Senior District Judge.

Plaintiffs, Amoco Production Company ("Amoco") and Atlantic Richfield Company and Vastar Resources ("ARCO/Vastar"), individually filed complaints seeking a declaratory judgment and injunction against Defendants, the United States Department of the Interior ("DOI"), its Secretary

Bruce Babbit, and its Assistant Secretary Sylvia Baca.[1] Plaintiffs seek to enjoin DOI decisions relating to the determination of royalties due on the production of coalbed methane gas produced by Plaintiffs from certain federal leases.

Currently before the Court are the parties' Motions for Summary Judgment. Plaintiffs ask the Court to declare the DOI decisions invalid and unlawful and to enjoin the DOI from implementing or enforcing its decisions. Defendants oppose Plaintiffs' motions and argue that they are entitled to judgment as a matter of law. Also before the Court is an amicus brief filed by the Southern Ute Indian Tribe ("Tribe") in support of Defendants.

## BACKGROUND

Plaintiffs, Amoco and ARCO/Vastar produce coalbed methane gas as lessees under federal oil and gas mineral leases in the San Juan Basin of northwestern New Mexico. The Minerals Leasing Act ("MLA") governs the terms of federal oil and gas leases, including the leases involved in this case. 30 U.S.C. §§ 181-287 (2003). The MLA was intended by Congress to "promote wise development of [ ] natural resources and to obtain for the public a reasonable financial return on assets that 'belong' to the public." *California Co. v. Udall*, 296 F.2d 384, 388 (D.C. Cir. 1961). In return for the privilege of producing coalbed methane gas on federal land, the MLA requires lessees to pay royalties based on the value of the production.

Coalbed methane gas, such as that produced by Plaintiffs, differs from conventional natural gas in that it contains significantly higher levels of carbon dioxide ($CO_2$). $CO_2$ reduces the value per unit of volume of natural gas because it has no energy value. As a result, $CO_2$ is generally

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[1] After taking office, Secretary Gale Norton was substituted for Bruce Babbit and Assistant Secretary Wallace P. deWitt was substituted for Sylvia V. Baca.

removed from the gas after it is extracted and gas transportation pipelines typically have quality specifications limiting the amount of $CO_2$ allowed in the gas stream. In some instances, $CO_2$ is recovered after removal and sold as a separate product, however that is not the case here.

On April 22, 1996, the Associate Director for Royalty Management, MMS, issued a letter to producers of coalbed methane gas ("Dear Operator Letter") containing guidelines for calculating the proper payment of royalties and correct reporting of production. The letter responded to questions received by MMS from producers operating in the vicinity of New Mexico's San Juan Basin, a group of producers that includes Plaintiffs. The guidelines contained in the Dear Operator Letter apply specifically to circumstances in which $CO_2$ is removed from coalbed methane gas and vented into the air rather than being processed and sold as a separate product.

The Dear Operator Letter echoed internal guidelines contained in a December 7, 1995 MMS memorandum ("December Memorandum") that also addressed the valuation of coalbed methane gas production. The December Memorandum in turn was issued following a November 2, 1995 meeting of the MMS Royalty Policy Board during which interested parties, including producers, offered alternative valuation and reporting methods for coalbed methane. The valuation policy set forth in the December Memorandum was a modified version of that presented by the MMS and the State of New Mexico during the November meeting.

On May 22, 1996, ARCO/Vastar appealed the guidelines contained in the Dear Operator Letter, but the appeal was returned because the letter itself was not a final decision of the MMS Director. MMS advised ARCO/Vastar that an appeal would be appropriate in the event lessees were ordered to take action to correct any noncompliance with the letter's guidelines. Subsequently, the State of New Mexico audited both Plaintiffs' production and royalty reporting and deter-

mined that, in fact, ARCO/Vastar and Amoco were not in compliance with the guidelines contained in the Dear Operator Letter. Based on the results of the New Mexico audit, the MMS issued the decision and orders that form the basis of Plaintiffs' Complaints.

***ARCO/Vastar's Complaint***

ARCO/Vastar appeals the consolidated decision of Assistant Secretary Sylvia V. Baca issued on March 24, 2000 ("ARCO/Vastar Decision"), which largely affirmed two decisions of the MMS relating to the calculation of royalties due on the sale of coalbed methane gas produced from federal leases held by ARCO/Vastar. The first decision was an MMS order issued on January 22, 1997 ("January Order") finding that ARCO/Vastar incorrectly calculated the royalties due on sales between 1989 and 1996. Upon review of deductions allowable under applicable regulations and the guidelines contained in the December Memorandum, the MMS determined that ARCO/Vastar erroneously took deductions for certain transportation and processing costs related to the transportation and removal of $CO_2$. As a result, the January Order directed ARCO/Vastar to pay past due royalties of $782,373, to recalculate the royalties due on certain leases in the San Juan Basin during the audit period, and to pay any additional royalties found to be due. The January Order further stated that late payment interest would be calculated and assessed pursuant to 30 C.F.R. § 218.102 (1996) upon receipt of any additional royalties due.

The second decision addressed by the ARCO/Vastar Decision was a decision by the MMS Royalty Valuation Board ("RVD Decision") issued on July 14, 1997 which denied a request for an extraordinary processing cost allowance. ARCO/Vastar had requested approval for an extraordinary processing cost allowance for the costs of removing $CO_2$ from coalbed methane gas produced from a federal lease and treated at a particular treatment facility. Based on

applicable regulations, the December Memorandum and the Dear Operator Letter, the Royalty Valuation Board rejected ARCO/Vastar's argument that the composition of the gas stream, plant design and associated costs justified the requested allowance.

Because the January Order and the RVD Decision raised overlapping issues related to the definition of marketable condition and extraordinary processing costs, the Assistant Secretary consolidated ARCO/Vastar's appeals of the two decisions. The ARCO/Vastar Decision largely upheld both the January Order and the RVD Decision and addressed four issues: (1) whether the cost of $CO_2$ removal is necessary to place the gas in marketable condition or allowable as an extraordinary processing cost allowance; (2) whether costs incurred to transport the coalbed methane gas are deductible; (3) whether the April 22, 1996 Dear Operator Letter violates the Administrative Procedure Act; and, (4) whether late payment interest is applicable to royalties deemed deficient for prior periods.

***Amoco's Complaint***

Amoco appeals the Assistant Secretary's decision of September 12, 2000 ("Amoco Decision"), which denied (with slight modifications) Amoco's appeal of a May 27, 2000 MMS Order ("May Order") directing Amoco to pay additional royalties of $4,117,607, to conduct a restructured accounting of certain federal and Indian leases, and to pay any additional royalties found to be due. The Assistant Secretary addressed four issues in the Amoco Decision: (1) whether $CO_2$ removal is necessary to place the gas at issue in marketable condition; (2) whether the costs of transporting excess $CO_2$ is deductible when coalbed gas is treated away from the lease; (3) whether the April 22, 1996 Dear Operator Letter violates the Administrative Procedure Act; and, (4) whether MMS can collect royalties that

become due more than six years before the date of the order to pay.

Since ARCO/Vastar and Amoco's appeals raise common issues their Motions for Summary Judgment were consolidated for briefing purposes. Plaintiffs argue that the guidelines contained in the Dear Operator Letter are invalid because the letter violates the Administrative Procedure Act. They further argue that $CO_2$ removal is not necessary to place coalbed methane gas in marketable condition and that they are entitled to transportation allowances for transporting $CO_2$ from the wellhead to treatment facilities where $CO_2$ is removed. Plaintiffs additionally assert separate claims. ARCO/Vastar argues that it is entitled to an allowance for extraordinary processing costs and that DOI improperly assessed late payment interest on overdue royalties. Amoco argues that the statute of limitations prohibits the collection of royalties after six years. The Court will first address Plaintiffs' common claims and then move to the individual claims.

## APPLICABLE LAW

### *Summary Judgment Standard and Standard of Review*

Summary judgment is appropriate when the record shows that "there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Fed. R. Civ. Pro. 56(c) (2003). The Court must set aside the Assistant Secretary's decisions under the Administrative Procedure Act ("APA") if they are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with the law." 5 U.S.C. 706(2)(A) (1996). When Congress has not spoken to the specific question at issue a court will defer to an agency's interpretation of a statute it is entrusted to administer so long as [is] reasonable and "is based on a permissible construction of the statute." *Chevron U.S.A., Inc. v. Natural Resources Defense Council*, 467 U.S. 837, 842-45, 104 S.Ct. 2778, 81 L. Ed. 2d 694 (1984).

Deference to the Assistant Secretary's decisions is appropriate in this case because Congress plainly delegated broad authority to the DOI "'to prescribe necessary and proper rules and regulations and to do any and all things necessary to carry out and accomplish the purposes of [the Minerals Leasing Act]' . . . [which includes] collecting royalties and determining the methods by which they are calculated." *Independent Petroleum Ass'n of America v. DeWitt*, 279 F.3d 1036, 1039 (D.C. Cir. 2002) ("*IPAA*") (quoting 30 U.S.C. § 189). Moreover, deference is regularly accorded to agency decisions relating to mineral leases and royalty valuations. *IPAA*, 279 F.3d at 1040 (citing numerous cases in which courts deferred to agency construction of royalty regulations).[2]

***The Mineral Leasing Act, the Federal Oil and Gas Royalty Management Act and Related Regulations***

The MLA invests the Secretary of the Department of the Interior with the authority to "prescribe necessary and proper rules and regulations and to do any and all things necessary to carry out and accomplish the purposes of [the MLA]." 30 U.S.C. § 189 (1986). The Minerals Management Services ("MMS"), a division within the DOI, administers the MLA and manages royalty payments.

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[2] As this Circuit has noted, arbitrary and capricious review under the APA and the *Chevron* deference standard of review "overlap at the margins." *Independent Petroleum Ass'n of America v. Babbitt*, 92 F.3d 1248, 1258 (D.C. Cir. 1996) ("*Babbitt*"); *Arent v. Shalala*, 70 F.3d 610, 615 (D.C. Cir. 1995); *Nat'l Ass'n of Regulatory Util. Comm'rs v. ICC*, 41 F.3d 721, 728 (D.C. Cir. 1994). The heart of the matter in this case is whether the Assistant Secretary's decisions interpreting royalty valuation statutes and regulations were reasonable and consistent with the purpose of the Mineral Leasing Act. Understanding that an unreasonable interpretation is functionally equivalent to an arbitrary or capricious interpretation, analytically, the Court will apply the *Chevron* deference standard of review.

The Federal Oil and Gas Royalty Management Act of 1982 ("FOGRMA") was enacted by Congress upon finding that "the system of accounting with respect to royalties and other payments due and owing on oil and gas produced from such lease sites is archaic and inadequate." 30 U.S.C. § 1701(a)(2) (1986). The purpose of FOGRMA is to:

> clarify, reaffirm, expand, and define the responsibilities and obligations of lessees, operators, and other persons involved in transportation or sale of oil and gas from the Federal and Indian lands . . . [and] to clarify, reaffirm, expand, and define the authorities and responsibilities of the Secretary of the Interior to implement and maintain a royalty management system for oil and gas leases on Federal lands . . . .

30 U.S.C. § 1701(b)(1), (2) (1986).

FOGRMA directs the Secretary of DOI to "audit and reconcile, to the extent practicable, all current and past lease accounts for leases of oil or gas and take appropriate actions to make additional collections or refunds as warranted." *Id.* at § 1711(c)(1) (1986). The Secretary may delegate all or part of this authority to a State upon written request. *See* 30 U.S.C. § 1735(a) (2003).

As noted previously, the MLA requires federal lessees to pay royalties in return for the privilege of mining federal lands. The calculation of royalties is governed by a labyrinth of interrelated statutes and regulations. The MLA requires lessees to pay a royalty "at a rate of not less than 12½ % in amount or value of the production removed or sold from the lease." 30 U.S.C. § 226(b)(1)(A) (2003). The "value of production" is defined by the so-called "gross proceeds" rule which provides that, for royalty purposes, the value of production shall under no circumstances be less than the gross proceeds earned by the lessee, minus certain allowances for transportation and processing. 30 C.F.R. § 206.153(h) (2002); 30 C.F.R. § 206.157(a) (2002); 30 C.F.R.

§ 206.158 (2002). "Production," as that term is used in the phrase "value of production," is production in marketable condition. *California Co.*, 296 F.2d at 388.

The availability of transportation and processing allowances implicitly recognizes that the government should share in certain costs of production. However, lessees are required to assume the entire cost of placing gas in "marketable condition" and marketing the gas for the mutual benefit of the government and lessee. 30 C.F.R. § 206.153(i) (2002). "Marketable condition" is a term of art defined for purposes of valuation as "lease products which are sufficiently free from impurities and otherwise in a condition that they will be accepted by a purchaser under a sales contract typical for the field or area." 30 C.F.R. § 206.151 (2002). By definition then, "marketable condition" is a fluid concept, wholly dependent on the particular facts of each case.

The marketable condition rule is pivotal in the calculation of royalties because it affects the determination of a lessee's gross proceeds, and therefore the value of production. When value "is determined by a lessee's gross proceeds, that value will be increased to the extent that the gross proceeds have been reduced because the purchaser, or any other person, is providing certain services the cost of which ordinarily is the responsibility of the lessee to place the residue gas or gas plant products in marketable condition or to market the residue gas and gas plant products." 30 C.F.R. § 206.153(i). In other words, royalties are due on the value of the gas in a certain condition—marketable condition—whether or not the producer pays the necessary conditioning costs directly or indirectly. The $64,000 question in this case is identifying what condition is "marketable condition" with respect to the gas produced by Plaintiffs.

## DISCUSSION

***The Payor Letter Does Not Violate the Administrative Procedure Act***

Plaintiffs argue that the DOI applied the Dear Operator Letter of April 22, 1996 as an agency rule in violation of the APA. For purposes of the APA, a rule is defined as "the whole or part of an agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy or describing the organization, procedure, or practice requirements of an agency." 5 U.S.C. § 551(4) (1991). Agency rules are subject to notice and comment, meaning that an agency must publish a proposed rule in the Federal Register and allow interested parties sufficient time to submit comments. 5 U.S.C. § 553 (1996). Interpretive rules, general statements of policy and rules of agency organization, procedure or practice are exempt from notice and comment procedures. *See id.* at § 553(b)(3)(A). An agency rule issued without notice and comment will be set aside as unlawful unless it falls within one of the three exceptions. 5 U.S.C. § 706(2)(D) (1996).

In both the ARCO/Vastar Decision and the Amoco Decision, the Assistant Secretary determined that the Dear Operator Letter is an interpretation of existing regulations and that the procedural requirements of the APA were therefore inapplicable. *See* ARCO/Vastar Decision at 19; Amoco Decision at 20 (citing *Shalala v. Guernsey Memorial Hospital*, 514 U.S. 87, 115 S.Ct. 1232, 131 L. Ed. 2d 106 (1995)). She further found that the MMS properly applied the valuation regulations as explained by the Dear Operator Letter and noted that the decisions of March 24, 2000 (ARCO/Vastar Decision) and September 12, 2000 (Amoco Decision) modified any inconsistencies between the MMS decision and the regulations that may have existed.

Plaintiffs argue that the Assistant Secretary erred and that the Dear Operator Letter is a substantive rule which

must be set aside because it was never subject to notice and comment. Alternatively, Plaintiff's argue that even if the Dear Operator Letter is not a substantive rule, i.e., it falls within one of the APA's three exceptions, notice and comment was nonetheless required because the Letter effected a change in existing law or policy. Defendants counter that the Dear Operator Letter was not subject to notice and comment because it is not binding on the agency and because it did not introduce a significant change in existing law.

In circumstances substantially similar to the instant case, this Circuit held that an interpretive letter issued by the MMS did not constitute a rule and was therefore not subject to notice and comment. *Babbitt*, 92 F.3d at 1256-57. In *Babbitt*, the Associate Director of Royalty Management, MMS, issued a letter clarifying its treatment of settlement payments. It was part of a series of adjustments made by MMS in the face of fundamental changes in the structure of the natural gas industry and subsequent judicial decisions interpreting legislative intent and agency action. Specifically, the letter at issue in *Babbitt* related to the determination of royalties due on settlement payments made by pipeline purchasers of natural gas to lessees in return for contract amendments or buyouts. The District Court held, and the Court of Appeals affirmed, that the letter itself did not constitute a rulemaking because "nothing in the DOI's procedures vests authority in the Associate Director of the MMS [the letter's author], or even the Director, to issue proclamations binding on the agency . . . [q]uite simply, the May 1993 letter is not an 'agency statement' with 'future effect' since it did not bind the agency in any way." *Babbitt*, 92 F.3d at 1256 (affirming the District Court's unpublished decision in *Independent Petroleum Ass'n of America v. Babbitt*, 1995 WL 431305 at *4 (D.D.C. June 14, 1995)).

The Dear Operator Letter at issue in this case was likewise issued by the Associate Director for Royalty Manage-

ment, MMS, and therefore for the same reasons, it can no more bind the agency than the letter at issue in *Babbitt*. To the extent that the ARCO/Vastar Decision and the Amoco Decision conflict with the above analysis, they are overturned. Nevertheless, the outcome is the same; the Court will not set aside the Dear Operator Letter because it is not a rule and it was therefore not subject to notice and comment.

***Plaintiffs' Coalbed Methane Gas Is Not in Marketable Condition at the Wellhead***

In their respective appeals to the Assistant Secretary, ARCO/Vastar and Amoco each asserted that the marketable condition rule only requires lessees to place gas in the physical condition necessary to market it under contracts typical for the field or area immediately surrounding the wellhead. Plaintiffs argued that their gas is in marketable condition in its natural state because it can be sold at the wellhead, and therefore they are not required to condition gas for downstream markets. Plaintiffs additionally argued that the MMS's requirement of conditioning gas to the interstate pipeline standard of 2% $CO_2$ was arbitrary and capricious. The Assistant Secretary flatly rejected both arguments.

Though the Assistant Secretary's Decisions are somewhat circuitous, the underlying rational[e] is sound. After reviewing Plaintiffs' gas sales, she found that most of the gas produced by Plaintiffs from the field or area was conditioned to reduce the level of $CO_2$ because it was sold for use in distant markets.[3] This was true, the Assistant Secretary noted, whether gas was purchased at the wellhead in its natural state and subsequently conditioned by the purchaser, or purchased at the tailgate of a treatment plant

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[3] The Assistant Secretary noted that only about 10% of the production from the area was utilized in its untreated form. *See* Amoco Decision at 7-8, n. 11; ARCO/Vastar Decision at 5, n. 7 and 7, n. 9.

after conditioning. The Assistant Secretary further noted that the purchase price of gas purchased at the wellhead in its natural condition was reduced to offset costs incurred by the purchasers to transport and condition gas to remove $CO_2$. In other words, the Assistant Secretary determined, contracts typical for the field or area involve gas with reduced $CO_2$ levels, whether the gas is purchased in that condition or whether purchasers perform the conditioning themselves in return for a reduced price, i.e., "[t]he fact that some purchasers are willing to purchase gas prior to conditioning and perform the conditioning themselves does not alter the finding that the gas needs to be conditioned." *See* ARCO/Vastar Decision at 5; Amoco Decision at 9. The Assistant Secretary concluded therefore that gas from the area must have a reduced level of $CO_2$ to be in marketable condition, and that producers cannot "alter the form of their sales arrangements in order to force the lessor to share in [their] costs to place the product in marketable condition." *See id.* Finally, based on her observation that most of the coalbed methane gas produced by Plaintiffs was sold for use outside the area of production, the Assistant Secretary agreed with MMS that the pipeline standards for $CO_2$ content effectively established the marketable condition standard.[4]

In the instant appeal, Plaintiffs again argue that gas is in marketable condition at the wellhead in its natural state and that the Assistant Secretary erred in finding otherwise. First, to be clear, Plaintiffs do not question the fact that they must bear the cost of placing the gas in marketable condition. Rather, they argue that the gas at issue is in marketable condition at the wellhead in its natural state as

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[4] The Assistant Secretary modified the ARCO/Vastar January Order and the Amoco May 27, 1997 Order to the extent that they directed Plaintiffs to recalculate royalties using pipeline quality standards that allowed variable amounts of $CO_2$ (1-3%) in the gas stream.

evidenced by the existence of wellhead sales. In other words, Plaintiffs would have the Court hold that the simple fact that gas can be sold at the wellhead demonstrates that it is in marketable condition. Defendants argue that the existence of wellhead sales is not determinative of whether gas is in marketable condition. Both parties rely upon *California Co.* for support of their position.

*California Co.* holds that the marketable condition rule requires the lessees to pay royalties on the costs of placing gas in marketable condition. *California Co.*, 296 F.2d at 388. Calco, a lessee producing oil and gas on federal leases, executed a contract under which it agreed to sell gas "in its natural state suitable for pipeline transmission" at a particular price. *California Co.*, 296 F.2d at 386. Although some of the gas produced by Calco met pipeline requirements in its natural state, some gas required compression or other conditioning to meet the pipeline requirements. *See id.* Calco acknowledged its obligation to market gas removed from the lease, but claimed that it was required to pay royalties only on the price of the gas minus the cost of conditioning. *See id.* at 386-87. Stated another way, Calco argued that it was not required to pay royalties on the cost of conditioning the gas. The Department of Interior thought otherwise. *See id.* at 387.

As described *infra*, the royalty valuation statute requires lessees to pay a royalty of 12½ % of the value of production removed or sold from the lease. 30 U.S.C. § 226(b)(1)(A).[5] In reviewing the agency's decision in *California Co.*, the Court of Appeals focused on the phrase "value of production" and asked whether "production" refers to the raw product regardless of its condition, or the product conditioned for the market in which it is being sold.

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[5] Though the statute has been amended since *California Co.* was decided, the substance of this particular provision has remained unchanged.

*California Co.*, 296 F.2d at 387. The Secretary of the Department of Interior construed "production" as meaning gas conditioned for market because lessees were obliged to market the product at no cost to the government. *See Id.* at 388. Ultimately, the Court of Appeals for the District of Columbia Circuit agreed, and as a result, Calco was required to pay royalties on the costs of conditioning the gas. The Court of Appeals prefaced their conclusion with a particularly salient observation:

> [t]heoretically, any gas—any "production"—is "marketable." We can assume that, if the price were low enough to justify capital expenditures for conditioning equipment, someone would undertake to buy [gas in its natural condition]. A lessee who sold unconditioned gas at such a price would, in a rhetorical sense, be fulfilling his obligation to "market" the gas, and by thus saving on overhead he might find such business profitable. There is a clear difference between "marketing" and merely selling. For the former there must be a market, an established demand for an identified product. We suppose almost anything can be sold, if the price is no consideration. In the record before us there is no evidence of a market for the gas in the condition as it comes from the wells.

*Id.* at 387-88.

The distinction between "marketing" and merely "selling" is especially relevant given the facts of this case and the analysis underlying the Assistant Secretary's conclusion that the market for the gas at issue was for gas with reduced levels of $CO_2$. Based on typical sales contracts for the gas at issue, the Assistant Secretary determined that there was a very limited market for gas in its natural condition, which market consisted of a small local community capable of utilizing gas in spite of high levels of $CO_2$. The typical sales contract for gas produced in the area was one in which purchasers demanded gas suitable for the actual

market which was distant from the production area. Thus, the actual market was for gas having low levels of $CO_2$, whether purchasers bought the gas at a reduced price and conditioned it themselves, or whether they purchased the gas at the tailgate of a treatment plant after conditioning.

The cases cited by Plaintiffs are consistent with the holding of *California Co.* and provide no support for their position. In *Xeno, Inc.*, 134 I.B.L.A. 172 (1995), plaintiff, Xeno, together with other lessees from the same producing area, formed a joint venture to purchase gas at the wellheads and resell it to a third party after gathering and compression. *Xeno*, 134 I.B.L.A. at 173-4. Xeno paid royalties on the gross proceeds it received from the joint venture. *See id.* at 174. The State of Montana reviewed Xeno's royalty payments and determined that Xeno improperly deducted gathering and compression charges from its gross proceeds because it had valued lease production on the gross proceeds received from sales to the affiliated joint venture rather than the value established by the arms-length agreement between the affiliated joint venture and the third party. *See id.* The agency agreed with the State of Montana's audit and assessed additional royalties. *See id.* Given the circumstances surrounding the joint venture's formation, the agency presumed that the sole purpose of the affiliated joint venture was to relieve Xeno and the other producers of the cost of gathering and compressing the gas, thereby reducing the amount of gross proceeds against which royalties would be collected. *See id.* at 175. The agency explained that the producers could not reduce the value of the gas for royalty purposes by gathering and compression costs that were necessary to put the gas in marketable condition, regardless of whether the gathering and compression was performed before or after being sold to the joint venture. *See id.*

Upon review, the administrative judge determined that the MMS incorrectly determined that gathering and com-

pression were necessary *per se* to place the gas in marketable condition. *Xeno*, 134 I.B.L.A. at 182. The administrative judge found no evidence in the record of any analysis by the MMS of what constituted marketable condition for the gas at issue. *See id.* This was in stark contrast to substantial evidence provided by Xeno of competing offers from firms other than the affiliated joint venture to purchase gas at the wellhead prior to gathering or compression for similar or higher prices. *See id.* at 182-83. Thus, "unlike the record in *California Co.* there [was] evidence of a market for the gas at the wellhead." *Id.* at 183. The existence of competing offers to buy gas at the wellhead indicated that there was in fact a market for the gas at the wellhead in its natural condition and that gathering and compression were not necessary to place the gas in marketable condition. Therefore the gathering and compression costs were properly excluded from Xeno's royalty calculation. *See id.*

The Tenth Circuit approved the rationale of *Xeno* in *Amerada Hess Corp. v. Dept. of Interior*, 170 F.3d 1032 (10th Cir.), though the outcome was not the same. The issue in *Amerada Hess* was whether royalties were owed on reimbursements received by the producers for certain production-related costs. *Amerada Hess*, 170 F.3d at 1036. The court ultimately held that royalty was owed on such costs. However in arriving at its conclusion the court distinguished the case from *Xeno*, stating that "*Xeno* reached a different result because the producer company in that case showed that its gas was in marketable condition and could be sold directly from the wellhead . . . [plaintiff] has made no such showing here, and therefore cannot benefit from the DOI's ruling in *Xeno*." *See id.* at 1037.

Plaintiffs additionally rely upon *Beartooth Oil and Gas Co. v. Lujan*, No. 92-99 (D.Mont. Sept. 22, 1993) (vacating and remanding *Beartooth Oil and Gas Co.*, 122 I.B.L.A. 267 (1992)). In *Beartooth*, the plaintiff, Beartooth, sold gas at

the wellhead to Mesa, which in turn sold the gas to Mountain Fuel. *Beartooth*, slip op. at 2. None of the companies were affiliated and each of the sales agreements were arms length. *See id.* The price Mesa paid Beartooth (and on which Beartooth paid royalties) was based on the price Mesa received from Mountain Fuel, reduced by certain factors including the cost of compression for delivery to Mountain Fuel. Beartooth appealed the agency's order demanding royalties for the amount the Mesa/Mountain Fuel price was reduced for compression costs. *Beartooth*, slip op. at 2-3.

The court vacated and remanded the agency's decision because the agency failed to determine what constituted "marketable condition" for the gas at issue. The court found that the MMS acted arbitrarily and capriciously because it did not consider whether or not the contract for sales of the gas at issue was "typical for the field." *Beartooth*, slip op. at 4. Rather, as it did in *Xeno*, MMS assumed that gas was not in marketable condition unless it was compressed. *See id.* at 5. The Court recognized in *Beartooth* that:

> Mesa may or may not be performing conditioning necessary to place Beartooth's gas into 'marketable condition.' However, until the IBLA first establishes what specifically constitutes 'marketable condition' for gas produced from the lease, it is arbitrary and capricious to conclude the gas as sold to Mesa was not in marketable condition.

*Id.* at 10.

Plaintiffs argue that the foregoing cases stand for the premise that gas is in marketable condition at the wellhead simply because it is sold at the wellhead. However, this construction is too narrow. In both *Xeno* and *Beartooth*, the agency's determination that gas was not in marketable condition at the wellhead was overturned because the agency failed to determine what constituted marketable

condition under the particular circumstances of the case—not because the gas was in marketable condition at the wellhead. The existence of wellhead sales are one factor to consider in identifying marketable condition, but it is not the determinative factor, in part because it overlooks the plain language of the applicable regulations.

The marketable condition rule anticipates and prohibits the type of arrangements alluded to in *California Co.* and which the agency mistakenly assumed existed in *Xeno*, wherein producers offer reduced prices to purchasers who in turn incur the costs of placing gas in marketable condition. Specifically, the rule requires lessees to

> place gas in marketable condition and market the gas for the mutual benefit of the lessee and the lessor at no cost to the Federal Government. Where the value established under this section is determined by a lessee's gross proceeds, that value will be increased to the extent that the gross proceeds have been reduced because the purchaser, or any other person, is providing certain services the cost of which ordinarily is the responsibility of the lessee to place the gas in marketable condition or to market the gas.

30 C.F.R. § 206.152(i) (2002).

The Court's role is to decide whether the agency's interpretation and application of the "marketable condition" rule in this case is reasonable. After reviewing the evidence presented by the parties and the marketable condition rule, the Assistant Secretary determined that in this case, the gas at issue is not marketable unless it has reduced levels of $CO_2$. Since lessees must bear the cost of placing gas in marketable condition, it makes no difference whether purchasers buy the gas at the wellhead for a reduced price or at the tailgate of a treatment plant after conditioning. The Court finds that, under the particular circumstances in this case, the Assistant Secretary's decision is a reasonable applica-

tion of the marketable condition rule. Therefore, Plaintiffs must pay royalties on the cost of conditioning the gas to reduce $CO_2$ levels.

***Limitations on Transportation Allowances Are Appropriate***

Though lessees are required to place gas in marketable condition at no cost to the government, they are permitted to deduct from the value of production certain reasonable and actual transportation costs. 30 C.F.R. § 206.156 (2002). Plaintiffs argue that the Assistant Secretary's determination that transportation costs for $CO_2$ levels in excess of pipeline quality standards are not deductible is in error because the transportation and removal of $CO_2$ is "directly related" to transportation of lease production.

As discussed *infra*, the gas at issue must have a reduced level of $CO_2$ to be in marketable condition; therefore, lessees bear the costs associated with removing excess $CO_2$. The Assistant Secretary observed that "transportation of the $CO_2$ to the treatment plant in this instance is a service that is inextricably tied to placing the gas in marketable condition because the $CO_2$ is extracted at the plant." ARCO/Vastar Decision at 15. She reasoned that the cost of transporting excess $CO_2$ from the wellhead to the conditioning facility was a marketing cost and could not be deducted as transportation costs.[6] As a result, the cost of transporting coalbed methane and 2% $CO_2$ from the wellhead to the conditioning plant was permitted as a transportation allowance and cost of transporting excess $CO_2$ was not.

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[6] Plaintiffs additionally challenge the Assistant Secretary's alternative rationale which turned on whether excess $CO_2$ is properly identified as a "waste" product or a "non-royalty" product. However, the Court need not address Plaintiffs' arguments on this issue since the Assistant Secretary's decision is affirmed on the grounds that marketing costs cannot be deducted as transportation costs.

The cases upon which Plaintiffs rely for their position are readily distinguishable from the facts of this case. *Marathon Oil Co. v. United States*, 604 F. Supp. 1375, 1378 (D. Alaska 1985), stemmed from a controversy between a lessee and MMS involving the proper method of valuing natural gas at the wellhead for royalty purposes. The marketable condition rule was not a factor in the court's finding that the costs of liquefying natural gas were incurred to facilitate transportation. *Marathon*, 604 F. Supp. at 1385-87. Similarly, in *Exxon Corp.*, 118 I.B.L.A. 221 (1991), the Interior Board of Land Appeals determined that dehydration of the gas at issue was not necessary to satisfy market specifications but rather was performed for the sole purpose of facilitating transportation. *Exxon Corp.*, 118 I.B.L.A. at 241. In contrast, $CO_2$ removal is essential in the instant case to place gas in marketable condition. That there exists a corollary benefit in reducing the level of $CO_2$ does not transform what is a marketing cost into a transportation cost. The Court therefore finds that the Assistant Secretary's application of the regulations relating to transportation allowances to the circumstances of this case is reasonable, and for that reason, Plaintiffs' appeal thereof is denied as to this issue.

***ARCO/Vastar Is Not Entitled to an Extraordinary Processing Allowance***

As described *infra*, lessees pay royalties on the value of production removed or sold from the lease. "Value of production" is defined by regulations promulgated by MMS and includes allowances that permit lessees to deduct certain transportation and processing costs from the royalty value. Lessees may not take deductions for costs incurred to place production in marketable condition or for processing lease production which is not royalty bearing. 30 C.F.R. § 206.158(d)(1) (2002). Lessees may however apply to MMS for an allowance for extraordinary processing costs, i.e., those shown to be extraordinary, unusual or un-

conventional as compared to standard industry conditions and practice. 30 C.F.R. 206.158(d)(2)(i). Guidelines issued by MMS on March 19, 1996, set forth the following factors MMS considers in evaluating an application for extraordinary processing costs: (1) the composition of the gas stream being processed; (2) the complexity of the gas plant design compared to conventional or typical gas processing plants, as well as the methods used to process the gas to remove elements or compounds from the gas; and (3) the unit costs incurred to recover the principal product, usually methane. *See* ARCO/Vastar Administrative Record, tab 23-2, MMS Guidelines for Extraordinary Processing Cost Recovery, March 19, 1996 ("March 19 Guidelines").

On April 29, 1997, Vastar requested approval for an extraordinary cost allowance for the cost of removing $CO_2$ from its gas stream. The RVD Decision denied Vastar's application because MMS determined that Vastar did not "compellingly demonstrate that the resource, plant design or unit costs are extraordinary, unusual or unconventional" and because "[r]egulations at 30 C.F.R. § 206.158(d)(1) (1996) disqualify a processing allowance for this case." *See* RVD Decision at 1. Vastar appealed the RVD Decision to the Assistant Secretary who, after reviewing the decision and considering the parties' arguments, agreed that ARCO/Vastar was not entitled to an extraordinary processing allowance.

ARCO/Vastar appeals the Assistant Secretary's decision arguing that it is arbitrary and capricious. ARCO/Vastar asserts that the Assistant Secretary ignored the DOI's own precedent because it had previously approved an extraordinary processing allowance for the Louisiana Land and Exploration Company for costs incurred in removing $CO_2$. ARCO/Vastar additionally argues that an extraordinary processing cost allowance is permitted under the March 19 Guidelines when gas plant products (in this case, $CO_2$) are vented into the air rather than being sold as a separate pro-

duct. Finally, ARCO/Vastar argues that coalbed methane gas as a product is eligible for an extraordinary cost allowance.

The ARCO/Vastar Decision is not arbitrary and capricious as the Assistant Secretary fully and carefully considered the prerequisites necessary for an extraordinary processing cost allowance before agreeing with MMS that ARCO/Vastar was ineligible. At the outset of the decision, the Assistant Secretary observed that ARCO/Vastar was not entitled to a processing allowance for the costs of $CO_2$ removal under 30 C.F.R. § 206.158(d)(1) because such conditioning was necessary to place the gas in marketable condition (a cost lessees must bear alone) and because the $CO_2$ was vented into the air rather than being captured and sold as a royalty bearing product. The Assistant Secretary then turned to the issue of whether $CO_2$ removal qualified as an extraordinary processing cost under 30 C.F.R. § 206.158(d)(2)(i) and the March 19 Guidelines.

The Assistant Secretary agreed with ARCO/Vastar that its gas is "atypical" due to the high $CO_2$ content, but stated that this determination alone was not dispositive, presumably because the design of the Val Verde plant and the process used to remove the $CO_2$ must also be considered. *See* ARCO/Vastar Decision at 12; *see also*, March 16 Guidelines. Though ARCO/Vastar attempted to distinguish the Val Verde plant from conventional plants by focusing on the type, concentration and amount of amine used and the amount of water required to remove $CO_2$ from the gas stream, the Assistant Secretary concluded that the use of amine in gas processing plants is common and the Val Verde plant itself was relatively simple compared to other conventional gas processing plants because its only function is to remove $CO_2$. *See id.* at 12. Finally, the Assistant Secretary was unable to evaluate whether ARCO/Vastar's costs were typical or extraordinary because ARCO/Vastar failed to provide standard industry costs for $CO_2$ removal.

Rather it simply argued that its cost of $0.0778 per Mcf to recover methane is "significant." *See id.* at 13.

ARCO/Vastar's argument that it is entitled to an extraordinary processing cost allowance because of the agency's decision regarding extraordinary processing cost allowances for Louisiana Land and Exploration Company ("LL & E") is entirely without merit. *See* ARCO/Vastar Administrative Record, tab 13-3, MMS letter to The Louisiana Land and Exploration Company, March 15, 1996 ("LL & E Letter"). First, the regulation requires lessees to apply to the MMS for an extraordinary processing cost allowance, which will be granted "only if the lessee can demonstrate that the costs are, by reference to standard industry conditions and practices, extraordinary, unusual, or unconventional." 30 C.F.R. § 206.158(d)(2)(i). In other words, extraordinary processing cost allowances are approved on a case by case basis and are necessarily dependent on the specific facts of each case.

Second, unlike ARCO/Vastar, LL & E demonstrated that not only its gas but also its plant design and costs were extraordinary, unusual or unconventional in comparison to standard industry conditions. LL & E's gas was atypical because it contained no natural gas liquids ("NGLs") and was comprised of 20% $CO_2$ and 12.6% hydrogen sulfide ($H_2S$). *See* LL & E Letter at 3. MMS noted that "[t]his gas is the only gas stream in the continental U.S. containing such high levels of both $CO_2$ and $H_2S$, with no NGLs."[7] *See id.* Further complicating matters was the fact that the gas

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[7] ARCO/Vastar argues that it is entitled to an extraordinary processing cost allowance because with respect to LL & E "the MMS relied on the absence of liquids in a gas stream for its finding that the gas was atypical and qualified for an extraordinary processing allowance." *See* Plaintiffs' Joint Memorandum of Points and Authorities in Support of Motions for Summary Judgment at 52. However, this is a misstatement as MMS plainly did not rely solely on the fact that LL & E's gas contained no NGL's.

produced by LL & E was significantly hotter than conventional gas streams. *See id.* The MMS found that the high temperature of the LL & E gas combined with its highly acidic composition necessitated a unique and complex processing unit. *See id.* In contrast, the Assistant Secretary noted that the amine process used in the Val Verde plant is "quite common" and the plant itself is "composed of only one part of what is considered a fairly complex natural gas processing plant." *See* ARCO/Vastar Decision at 12. Finally, LL & E provided both its own processing costs and typical industry costs of processing acidic gas streams, enabling MMS to compare the two and determine that in fact LL & E's processing costs were extraordinary. *See id.* at 4. ARCO/Vastar did not provide standard industry costs for recovering methane, but rather expected the Assistant Secretary to rely on its assertion that its costs were "significant."

ARCO/Vastar's remaining arguments are merely unsupported assertions. ARCO/Vastar does not explain why the March 16, 1996 Guidelines would permit an extraordinary processing cost allowance when gas plant products such as $CO_2$ are vented into the air rather than being sold as a separate product. Nor does ARCO/Vastar describe why coalbed methane gas as a product is eligible for an extraordinary cost allowance.[8] As a result, ARCO/Vastar's appeal is denied as to this issue.

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[8] ARCO/Vastar consistently compares its gas to non-coalbed natural gas in order to justify an extraordinary processing allowance. However, MMS sensibly explained in the RVD Decision why such a comparison is inapplicable:

> [n]atural gas has diverse characteristics in terms of geologic setting, reservoir properties, operational requirements and particularly composition. Although one may classify natural gas into certain categories, such as sweet gas, sour gas, wet gas, dry gas, associated gas or even coalbed gas, each gas occurrence has individual characteristics that differentiate it to some degree

***Late Payment Interest Is Due on Additional Royalties***

In the January Order, MMS stated that late payment interest would be calculated and assessed upon receipt of payment of additional royalties. *See* January Order at 8. The Assistant Secretary sustained the assessment of late payment interest in the ARCO/Vastar Decision because she determined that it was supported by longstanding precedent. *See* ARCO/Vastar Decision at 19.

The government's right to interest on late royalty payments is statutorily recognized in FOGRMA, which states that:

> in the case of oil and gas leases where royalty payments are not received by the Secretary on the date that such payments are due, or are less than the amount due, the Secretary shall charge interest on such late payments or underpayments at the rate applicable under section 6621 of Title 26. In the case of an underpayment or partial payment, interest shall be computed and charged any on the amount of the deficiency and not on the total amount due.

30 U.S.C. § 1721(a) (2003).

Likewise, the implementing regulation issued by MMS states that "an interest charge shall be assessed on unpaid and underpaid amounts from the date the amounts are due." 30 C.F.R. § 218.54(a) (2002). The imposition of late payment interest charges is intended to compensate the government for the time value of money due to it but not timely paid. *See Meridian Oil, Inc.*, 140 I.B.L.A. 135, 143

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from another. In this respect it can be argued that each natural gas is unique in some manner.

*See* RVD Decision at 3-4.

In other words, the real question is not whether coalbed methane gas is atypical (which the Assistant Secretary determined it was), but whether the coalbed methane gas produced by Vastar is atypical or unusual.

(1997). The language of the statute and implementing regulation indicates that the assessment of late payment interest is not discretionary.

ARCO/Vastar argues that "imposition of late payment interest would be inequitable" and urges the Court to relieve it of late payment interest charges as the court did in *Jicarilla Apache Tribe v. Continental Oil Co.*, No. 76-430 (D.N.M. November 21, 1988) ("*Conoco*"). Plaintiff's reliance on the *Conoco* decision is misplaced however because it dealt with the payment of *prejudgment* interest and because the lessees in the case were ultimately required to pay *postjudgment* interest.

In *Conoco*, the court found, in relevant part, that lessees owed additional royalties in an amount to be calculated by the agency within a set time. The court declined to assess *prejudgment* interest at the time of its decision because it was not "appropriate on a debt which is unliquidated and incapable of calculation prior to judgment." *Conoco*, Findings of Fact and Conclusions of Law, May 13, 1998, at 17. Following the *Conoco* decision, the amount of royalties owed by the lessees was calculated and the MMS issued three Orders assessing additional royalties and corresponding late payment interest. The IBLA sustained the assessment of late payment interest on appeal. In its analysis, the IBLA reviewed 30 U.S.C. § 1721(a) and 30 C.F.R. § 218.54(a), and determined that "the court's denial of prejudgment interest [in *Conoco*] does not bar MMS from seeking postjudgment interest on those underpayments . . . [i]ndeed, MMS is statutorily required to do so." *Meridian Oil, Inc.*, 140 I.B.L.A. at 144.

As the IBLA observed in *Meridian*, the mandatory nature of the statutory and regulatory language pertaining to the payment of late payment interest speaks for itself, and for that reason, the Court will not set aside the Assistant Secretary's assessment of late payment interest.

***The Amoco Decision Does Not Violate the Statute of Limitations***

Amoco argues that the agency is barred from collecting royalties accrued more than six years prior to the May 27, 1997 Order by the statute of limitations set forth in 28 U.S.C. 2415(a):

> [s]ubject to the provisions of section 2416 of this title, and except as otherwise provided by Congress, every action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later . . . .

28 U.S.C. § 2415(a) (1994).

The Assistant Secretary denied Amoco's appeal on this issue stating that the statutory bar was inapplicable because the proceeding was an administrative appeal. *See* Amoco Decision at 21. Her decision was consistent with longstanding I.B.L.A. precedent. *See Foote Mineral Co.*, 34 I.B.L.A. 285, 306-308 (1978); *Anadarko Petroleum Corp.*, 122 I.B.L.A. 141, 148 (1992) (holding that § 2415(a) does not apply to administrative proceedings); *Meridian Oil, Inc.*, 140 I.B.L.A. 135, 145 (1997) (stating that "we have long ruled that statutes establishing time limitations for the commencement of judicial actions for damages on behalf of the United States do not limit administrative proceedings within the DOI").

In 1996, Congress amended FOGRMA by enacting a seven year statute of limitations on lease-related demands, specifically "a judicial proceeding or demand which arises from, or relates to an obligation, shall be commenced within seven years from the date on which the obligation becomes

due and if not so commenced shall be barred." 30 U.S.C. § 1724(b)(1) (2003). The amendment explicitly precludes the application of the statute of limitations set forth in 28 U.S.C. § 2415 to any obligation arising under FOGRMA. 30 U.S.C. § 1724(b)(3). Unfortunately, the provisions of the amended statute do not control this case because it relates to gas produced between January 1989 and August 1996; the seven year statute of limitations of § 1724(b)(1) applies only to oil and gas production occurring after its effective date of September 1, 1996. As a result, the Court must determine whether 28 U.S.C. 2415(a) bars the agency from collecting royalties due more than six years prior to the May 27, 1997 MMS Order.

The Court's inquiry must begin with the language of the statute itself. *Butler v. West*, 164 F.3d 634, 639 (D.C. Cir. 1999). In addition, the United States Supreme Court has held that "statutes of limitation sought to be applied to bar rights of the Government . . . must receive a strict construction in favor of the Government." *Badaracco v. Comm'r of Internal Revenue*, 464 U.S. 386, 391, 104 S.Ct. 756, 78 L. Ed. 2d 549 (1984) (quoting *E.I. Dupont De Nemours & Co. v. Davis*, 264 U.S. 456, 462, 44 S.Ct. 364, 68 L.Ed. 788 (1924)). Complicating matters is the existence of a circuit split as to whether 28 U.S.C. § 2415(a) applies to MMS orders to collect additional royalties.

Plaintiffs rely primarily upon a relatively recent en banc decision in which the 10th Circuit held that 28 U.S.C. § 2415(a) barred an MMS order directing lessees to pay additional royalties on production produced before September 1, 1996. *OXY USA, Inc. v. Babbitt*, 268 F.3d 1001 (10th Cir. 2001) ("*OXY USA II*").[9] *OXY USA II*

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[9] Plaintiffs additionally cite a decision by the United States District Court for the District of Alaska which applied § 2415(a) to an MMS order seeking additional royalties because it found such efforts "more analogous to actions at law for damages than to actions in

stemmed from a December 1996 order issued by MMS directing lessees to pay additional royalties for oil produced from federal leases between January 1980 and September 1983. *OXY USA II*, 268 F.3d at 1003-1004. Lessees filed suit in district court seeking a declaration that the claim for royalties was time barred by 28 U.S.C. § 2415(a). *See id.* The district court, relying on language in *Phillips Petroleum Co. v. Lujan*, 4 F.3d 858, 860 & n. 1 (10th Cir. 1993), determined that § 2415(a) barred the MMS order and granted summary judgment in favor of lessees.[10] *See id.* On appeal, a divided panel of the 10th Circuit Court of Appeals reversed, holding that § 2415(a) was inapplicable because MMS orders are not "actions" as contemplated by the statute. *OXY USA, Inc. v. Babbitt*, 230 F.3d 1178, 185-90 (10th Cir. 2000) ("*OXY USA I*").

The 10th Circuit granted a Petition for Rehearing and after a methodical analysis, concluded that "the statutory language, together with a forthright statutory scheme and purpose, clearly instruct that the six year statute of limitation[s] under 28 U.S.C. § 2415(a) applies to the MMS orders in this case." *OXY USA II*, 268 F.3d at 1005. Upon concluding that the statutory time bar of 28 U.S.C. § 2415(a) applied, the 10th Circuit vacated *OXY USA I* and affirmed the district court's order granting summary judgment to the lessees. *See id.* at 1008.

In the en banc decision, the 10th Circuit first considered the phrase "every action" in § 2415(a) and found it to be "patently broad" and ultimately inclusive of administrative

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equity for restitution." *Marathon Oil Co. v. Babbitt*, 938 F. Supp. 575, 578 (D. Alaska 1996).

[10] The court in *Phillips Petroleum v. Lujan* accepted without discussion the parties' agreement that 28 U.S.C. § 2415(a) applied to the government's effort to collect royalty underpayment and agreed with the parties that the oil and gas leases at issue were contracts. *Phillips Petroleum v. Lujan*, 4 F.3d at 860.

collection proceedings such as the MMS order at issue. *Id.* at 1005. The statute's subsequent reference to a "complaint" did not limit its application to formalized judicial proceedings, the 10th Circuit stated, in light of "the statute's obvious purpose to level the playing field between the government and private litigants by forcing the government to promptly assert its claims [and a] reading of the entire text of § 2415, including subsections (f) and (i)." *Id.* Subsection (f) allows the United States to assert, in an action against it, a counter claim or offset against a party under certain conditions. 28 U.S.C. § 2415(f). Subsection (i) permits the United States to collect a claim by means of administrative offset. 28 U.S.C. § 2415(i). The 10th Circuit found these provisions demonstrative of Congressional intent for "§ 2415(a) to encompass more than the filing of a 'complaint' in court." *Id.* at 1006.

Notwithstanding lessees' statutory obligation to make royalty payments on production from federal leases, the 10th Circuit concluded that the MMS royalty collection order was founded on contract. *See id.* at 1007. The Circuit next rejected the distinction recognized by the 5th Circuit in an unpublished decision between "contractual obligations," i.e., royalties due on production, and money damages, finding that it too narrowly construed the phrase "money damages." *See id.* at 1007-1008 (referring to the 5th Circuit's decision in *Phillips Petroleum Co. v. Johnson*, 1994 WL 484506 (5th Cir.) ("*Phillips Petroleum*")). The Circuit stated that *Bowen v. Massachusetts*, 487 U.S. 879, 108 S.Ct. 2722, 101 L. Ed. 2d 749 (1988), upon which the 5th Circuit relied in *Phillips Petroleum*, was "neither binding nor persuasive" and held that the MMS order was an action for money damages because it was "substantively indistinguishable from other government claims to recover money owed under contracts governed by the limitations period in § 2415(a)." *Id.*

Finally, the 10th Circuit determined that FOGRMA's seven year statute of limitations did not trigger the "except as otherwise provided by Congress" exception of 28 U.S.C. § 2415 "because [the FOGRMA limitation] applied only to oil and gas production occurring after its effective date of September 1, 1996." *Id.* at 1009. The 10th Circuit further reasoned that Congress would not have amended FOGRMA to include a statute of limitations if it believed that the provisions therein and the enacting regulatory scheme otherwise superceded 28 U.S.C. § 2415(a). *See id.*

Defendants argue that § 2415(a) cannot apply to this case because it is not a complaint or action brought by the United States for money damages. Defendants refer to the unpublished 5th Circuit decision in *Phillips Petroleum* holding that § 2415(a) did not apply to an MMS order to collect additional royalties because "actions that don't involve the filing of a complaint are not 'action[s] for money damages'" as contemplated by the statute. *Phillips Petroleum*, 1994 WL 484506, *1. In addition, as mentioned above, the 5th Circuit noted in *Phillips Petroleum* the distinction between "money damages," which generally refers to a sum of money used as compensatory relief, and the contractual obligations sought by the MMS, and held that "[s]uch contractual obligations cannot be considered compensatory." *Id.* (citing *Bowen v. Massachusetts*, 487 U.S. 879, 897, 108 S.Ct. 2722, 101 L. Ed. 2d 749 (1988)).

More persuasively however, Defendants also rely upon a decision by the United States District Court for the District of Columbia, which held that the limitation of § 2415(a) did not act as a time bar to an MMS order to collect additional royalties and associated interest. *Samedan Oil Corp. v. Deer*, 1995 WL 431307 (D.D.C.) *rev'd on other grounds*, *IPAA v. Babbitt*, 92 F.3d 1248, 1260 (D.C. Cir.) ("[b]ecause we conclude that DOI cannot collect any royalties on the settlement payment, it is unnecessary for us to consider appellant Samedan's statute of limitations claim"). At issue

in *Samedan* was a December 1993 MMS order directing the lessee to pay royalties due on production produced between February 1988 and November 1989. *Samedan* at *1. In October 1994, after the agency affirmed the order, the lessee filed suit in court seeking to enjoin the order. *See id.* The government filed a counterclaim to enforce the order in November 1994. *See id.* The lessee argued in *Samedan* that the six year statute of limitations of § 2415(a) barred the collection of royalties due prior to October 31, 1988 because the "complaint" to enforce an "action for money damages," i.e., the MMS order, was the government's November 1994 counterclaim. *See id.* at *3. As in this case, the government argued that § 2415(a) did not apply.

The district court first decided that the lease, while it referred to and incorporated certain statutes and regulations, was founded on contract as evidenced by numerous contractual provisions such as the lease term, royalty rate, timing and frequency of payments, and record-keeping and reporting requirements. *See id.* at *4-5. Though separately the terms were not determinative of the existence of a contract, together the district court found that they "are integral to an interpretation of the lease [and] are beyond mere backdrop for an incorporated statute . . . the statute and the regulations play an interstitial role in an otherwise self-contained document." *Id.* at *5.

The district court next agreed with the government's position that the additional royalties sought by the MMS were "not money damages because they are not compensatory, but rather something to which the government is already entitled under the terms of the lease." *See id.* at *5. Looking to the 5th Circuit's decision in *Phillips Petroleum* and the Supreme Court's decision in *Bowen v. Massachusetts*, 487 U.S. at 893, 108 S.Ct. 2722 (stating that "the fact that a judicial remedy may require one party to pay money damages to another is not sufficient reason to characterize the relief as 'money damages'"), the court held that

§ 2415(a) was inapplicable because "DOI's claim is not to recover damages; it is to collect royalties payable under the terms of the Samedan lease." *Id.* at *6.

The district court next turned to the term "action" as used by the statute in the phrase "action for money damages." The lessee in *Samedan* urged the district court to extend the term "action" to include administrative proceedings. *Samedan* at *7. The district court found the 5th Circuit's opinion in *Phillips Petroleum* controlling and declined the lessee's invitation, reasoning that:

> [o]nly if "action" includes administrative proceedings but "complaint" is confined to judicial pleadings, might Samedan prevail. That construction, however, violates the sense of the statute. Section 2415(a) states that "every action for money damages . . . shall be barred unless the complaint is filed within six years . . . ." Use of the definite article 'the' to modify 'complaint'—instead of the indefinite article 'a'—tells us that a particularized 'complaint' has been previously specified by context . . . it is clear that the antecedent of 'complaint' is 'action.'

*Id.*

The district court therefore held that "action" as used in § 2415(a) applied to "judicial but not to administrative proceedings," and that the judicial action before the court (i.e., the government's counterclaim for summary judgment to enforce the administrative order) was an action to enforce an administrative order, not to collect money damages. *Id.* at *7-9.

To summarize, although the MMS order was based on contract, the United States District Court for the District of Columbia held in *Samedan* that § 2415(a) was no bar to the MMS order because the government was not pursuing "money damages" and because the government's claim was not an "action" as those terms are used in the statute. *See*

*also, Vastar Resources, Inc. v. Armstrong*, No. 94-02040 (D.D.C. Aug. 27, 1997); *but see, Fina Oil & Chemical Co. v. Norton*, 209 F. Supp. 2d 246, 257 (D.D.C. 2002) (finding that the six year statute of limitations under § 2415(a) applied, but holding that it did not bar the action before the court because it was brought by the lessee) *rev'd on other grounds, Fina Oil & Chemical Co. v. Norton*, 332 F.3d 672 (2003).

The Court finds the logic underpinning the district court's decision in *Samedan* persuasive. Therefore, upon review of the statute and consideration of the facts of this case, the Court holds that § 2415(a) does not bar the collection of royalties due six years prior to the May 27, 1996 MMS Order in this case for the following reasons. First, as in *OXY USA II* and *Samedan*, the royalty claims at issue in this case arise from the lease, i.e., a contract. Nevertheless, the MMS Orders which Plaintiffs appeal do not seek money damages, but rather claim royalties due under the lease. *Samedan* at *6. Furthermore, the relationship between "action" and "complaint" in the statute indicates that the statute applies to judicial proceedings, not administrative orders. *Samedan* at *7. Finally, the statute plainly bars "every action for money damages *brought by the United States*." The action currently before the court was not brought by the United States, it is an appeal of administrative orders brought by Plaintiffs pursuant to the Administrative Procedure Act and other statutes. Moreover, unlike the circumstances in *Samedan*, the government has not filed a counterclaim to enforce the May 1997 Order. Therefore, Amoco's Motion for Summary Judgment is denied with respect to this issue.

## CONCLUSION

For the reasons set forth herein, in an accompanying Order, the Court will deny the Plaintiffs' Motions for

Summary Judgments and grant the Defendants' Motion for Summary Judgment.

## APPENDIX C

## UNITED STATES DISTRICT COURT, DISTRICT OF COLUMBIA

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AMOCO PRODUCTION COMPANY,
*PLAINTIFF,*

v.

SYLVIA V. BACA, ET AL.,
*DEFENDANTS.*

VASTAR RESOURCES, INC. AND ATLANTIC RICHFIELD COMPANY,
*PLAINTIFFS,*

v.

SYLVIA V. BACA, ET AL.,
*DEFENDANTS.*

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NOS. CIV.A. 00-02933 (WBB),
CIV.A. 00-01480 (WBB)

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Nov. 14, 2003.

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### ORDER

Upon consideration of the parties' cross motions for summary judgment and the entire record herein, for the reasons set forth in the accompanying Memorandum, it is on this 14th day of November, 2003, hereby

ORDERED that Plaintiffs' Motions for Summary Judgment are DENIED in their entirety, and is it further

ORDERED that Defendants Motion for Summary Judgment is GRANTED in its entirety.

/s/ William B. Bryant
Senior United States District Court Judge

## APPENDIX D

[Seal Omitted]

# United States Department of the Interior

**OFFICE OF THE SECRETARY**

**WASHINGTON, D.C. 20240**

February 27, 2001

**CERTIFIED MAIL**
**Return Receipt Requested**

Mr. Charles A. Breer
Attorney for Vastar Resources,
Inc. and Atlantic Richfield Company
370 17th Street - Suite 4700
Denver, Colorado 80201-0185

Re: MMS-97-0063-O&G
MMS-97-0191-O&G
ARCO/Vastar

Petition for
Reconsideration
Denied

Dear Mr. Breer:

Atlantic Richfield Company and Vastar Resources, Inc. (ARCO/Vastar, the Petitioner) petitioned the Department of the Interior (Department) for reconsideration of the March 24, 2000, decision (Decision) in the above-referenced appeals issued by Sylvia V. Baca, the Assistant Secretary for Land and Minerals Management.[1] The Decision denied, in part, the appeals and modified the Minerals Management Service's (MMS) order dated January 22, 1997 (Order), which directed ARCO/Vastar to pay additional royalties and

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[1] *See Atlantic Richfield Co.*, MMS-97-0063-O&G, MMS-97-0191-O&G (March 24, 2000), 22 Gower Federal Service, Royalty Valuation and Management, Rocky Mtn. Min. L. Found.

to perform a restructured accounting and pay additional royalties due. The Order applies to all of ARCO/Vastar's San Juan Basin Federal and Indian leases[2] producing coalbed methane that is transported and processed through the Val Verde System for the period January 1989 through August 1996 (audit period).

In the Decision, the Department determined that:

1) the cost of $CO_2$ removal was not deductible in determining the value of production for royalty purposes because

(a) placing the coalbed gas in marketable condition at no cost to the lessor is required by the valuation regulations, and

(b) the $CO_2$ removal at issue does not qualify for an extraordinary processing cost allowance under the valuation regulations;

2) the cost of transporting $CO_2$ in excess of the applicable mainline specifications is not deductible from the value of production for royalty purposes because the cost of transporting non-royalty-bearing production cannot be deducted from the value of royalty bearing production;

3) the interpretation of existing rules contained in MMS's April 22, 1996, Dear Operator/Payor Letter does not violate the Administrative Procedure Act; and

4) late payment interest is applicable to past-period deficient royalties.

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[2] The Order was modified by the Decision to eliminate from consideration the valuation of coalbed methane from any Indian leases. *See* Decision at 1. n.2.

ARCO/Vastar now assert in their petition for reconsideration that MMS's conclusions concerning the marketability of the gas at the wellhead and concerning ARCO/Vastar's obligation to assume the conditioning costs necessary to meet mainline standards are factually and legally wrong. Petition for Reconsideration (Petition) at 1-2. In support of their arguments, ARCO/Vastar rely on the decision in *Independent Petroleum Ass'n of America v. Armstrong*, 91 F. Supp. 2d 117 (D.D.C. 2000), *appeal filed*, Nos. 00-5404 and 00-5405 (D.C. Cir.) (*IPAA v. Armstrong*), and affidavits executed by Dr. Alfred L. Parker and Mr. Peter Mueller.[3] Petition at Exhibit B, Parker Affidavit; Petition at Exhibit C, Mueller Affidavit.

*Issue*

Is the information submitted by ARCO/Vastar sufficient to support its request for reconsideration?

*Analysis*

1. Does *IPAA v. Armstrong* apply?

ARCO/Vastar misconstrues the decision in *IPAA v. Armstrong*. The issues in *IPAA v. Armstrong* involved primarily whether the lessee may deduct so-called "downstream" marketing costs in determining royalty value. Treatment of gas to put it in marketable condition was not at issue in *IPAA v. Armstrong*. Even the plaintiffs in that case did not dispute the marketable condition obligation. *See IPAA v.*

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[3] The affidavits were filed by Amoco Production Company (Amoco) in a related coalbed methane case affecting some of the same leases as the instant case. Petition at 2, n.2. By letter dated June 2, 2000, counsel for Amoco transmitted a supplemental affidavit from Dr. Parker revising and correcting information included in Dr. Parker's March 27, 2000, affidavit.

*Armstrong*, 91 F. Supp. 2d at 123. Further, the District Court, in granting the government's motion to alter or amend under Rule 59(e), Fed. R. Civ. P., which the plaintiffs did not oppose in this respect, agreed that the lessee's duty to place gas in marketable condition was not challenged or affected by the ruling in that case.

Therefore, *IPAA v. Armstrong* provides no support for ARCO/Vastar's position or its petition for reconsideration.

2. Do the Parker and Mueller affidavits present new factual information regarding what constitutes marketable condition for the coalbed gas?

Essentially, ARCO/Vastar's argument concerning marketable condition has not changed. ARCO/Vastar now aver that the Department, in reaching its decision, relies on erroneous assumptions that are unsupported by evidence. ARCO/Vastar aver that "Dr. Parker's study provides direct, substantial evidence that (i) there is an active market for coalbed methane gas at the wellhead and (ii) coalbed methane is in marketable condition at the well. Id. ¶¶ 66-70." Petition at 2. ARCO/Vastar argue that Dr. Parker's study provides additional evidence that refutes MMS's determination when it previously analyzed this issue.

Dr. Parker's survey indicates that what he calls "substantial" volumes of coalbed gas are typically priced and sold at the wellhead. There are a number of flaws in his assertions. First, the identification of numerous coalbed gas transactions in which a producing entity sells or transfers to a wholly-owned or wholly-commonly-owned trading or marketing entity adds no relevant information about the marketability of untreated gas. Transfers between affiliates "at the wellhead" do not create a market for untreated gas or create contracts for the sale of gas that are "typical" for the field or area. ARCO/Vastar's argument would allow lessees to create a loophole that would swallow the market-

able condition rule by the simple device of inter-affiliate transfers.

Nor does the identification of numerous sales from unaffiliated operators to these larger marketing and trading entities prove that there is a broad "market" for untreated gas or that the "typical" contract is for untreated gas. Marketability is not determined solely by saleability. An unmarketable hydrocarbon product almost always can be sold for a lower price—one that allows the initial purchaser to recover the costs of treatment when the production is resold. Indeed, Dr. Parker's affidavit implicitly admits this. In paragraph 50 of his affidavit, he states:

> Sales transactions which take place at the well are generally structured so that the buyer pays the producer a price for gas at the well which is generally equal to the San Juan Index Price (or some percentage thereof) *less costs incurred by the buyer between the well and the interstate pipeline.* (Emphasis added.)

Those costs incurred between the well and the interstate pipeline include the cost of $CO_2$ removal. Sale-for-resale transactions thus are not particularly informative regarding the actual marketability of the product.

Dr. Parker's affidavit further states in paragraph 52:

> Recognizing the capacity constraints found in the existing conventional system and the inefficiencies involved in the commingling of coal seam gas [which he stated in paragraph 51 is high in $CO_2$ content] and conventional gas [which he admitted in paragraph 51 is low in $CO_2$ content] in conventional gathering and gas processing systems. *El Paso refused to accept the large volume of coal seam gas* beginning to come on line in this period. (Emphasis added.)

He then notes in paragraph 53 that "[o]ther entities immediately stepped into the vacuum created by El Paso's unwillingness to accept coal seam gas on its conventional gathering system." Specifically, he observes, two entities built facilities "to gather *and treat* the new, large volumes of Coal Seam Gas in preparation for the interstate pipelines and offered these field transportation and *treating services to others for a fee.*" (Emphasis added.) In short, Dr. Parker's assertions, taken together, show that the bulk of untreated coalbed methane that is high in $CO_2$ content effectively is unmarketable.

Marketability is determined in part by whether the production is satisfactory for use by those who ultimately purchase it for use. The affidavits document that the wellhead coalbed gas sold and actually used in the untreated condition is approximately 90.5 MMcfd or 6.3 percent of daily New Mexico coalbed gas production.[4] Thus, over 90

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[4] The 90.5 MMcfd/6.3 percent was derived from figures provided by ARCO/Vastar with its SOR for the original appeal (*see* Exhibit 3 (Anderson Report), § III; Exhibit 4 (Edlund Affidavit), ¶ 4.a.-d.) and from the Petition (*see* Exhibit C (Mueller Affidavit). ¶¶ 54-59). This quantity does not include the volumes identified in these and related paragraphs where either the $CO_2$ content was five percent or less, *e.g.*, Red Cedar and Florida River systems gas (accounting for approximately 41.4 MMcfd or 2.9 percent), or the gas sales that were not specifically identified as gas used in its natural state with a high $CO_2$ content (*see, e.g.*, Exhibit B (Parker Affidavit), Exhibit ALP-13, Tbl. 1). The 90.5 MMcfd was compared to total New Mexico coalbed gas production of 1.435 MMcfd (*see* Exhibit B (Parker Affidavit), Exhibit ALP-13, Tbl. 1) rather than the 565 MMcfd used by Dr. Parker (*see Id.*) or the Val Verde Plant comparison of 800 MMcfd used in the Decision (*see Atlantic Richfield Co.*, MMS-97-0063-O&G, MMS-97-0191-O&G, 22 Gower Federal Service at 5, n.7, 7, n.9). Further, more than 75 MMcfd of the 90.5 MMcfd of untreated gas

percent of the daily New Mexico coalbed gas is treated for the removal of $CO_2$ and resold for use downstream. It was because the overwhelming percentage (90%) of coalbed gas is sold in a treated condition for the interstate market that the Assistant Secretary found that the gas at the wellhead is unmarketable without further basic treatment.[5] As determined by the Assistant Secretary, the amount of untreated wellhead sales is not "typical" within the meaning of the marketable condition regulation.

Much of Dr. Parker's affidavit actually consists of arguments against the marketable condition rule from a supposedly "economic" standpoint. While the views expressed are interesting, they are nevertheless contrary to settled law of gas valuation under Federal leases. The "marketable condition" rule has been uniformly sustained (*see e.g., Mesa Operating Ltd. Partnership v. Dep't of the Interior*, 931 F.2d 318 *reh'g denied* (5th Cir. 1991), *cert. denied*, 502 U.S. 1058 (1992)), and lessees must bear the costs of treatment to put production into marketable condition regardless of whether this particular affiant views untreated production as "marketable" in an "economic" sense. Further, ARCO/

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consists of Amoco's and others' post-production field and area uses in processing, treatment, and transportation of the gas (derived from figures provided by ARCO/Vastar with its SOR for the original appeal (*see* Exhibit 3 (Anderson Report), § III; Exhibit 4 (Edlund Affidavit), ¶ 4.a.-d) and from the Petition (*see* Exhibit C (Mueller Affidavit). ¶¶ 54-59)). In other words, a vast majority of the high $CO_2$ content gas used in its natural state is for transportation, treatment, and processing of the coalbed gas that must occur in the field or area.

[5] *See Atlantic Richfield Co.*, MMS-97-0063-O&G, MMS-97-0191-O&G, 22 Gower Federal Service at 7 (failure to meet pipeline standard renders production unmarketable).

Vastar's reliance on the Interior Board of Land Appeals' (IBLA's) decision in *Xeno, Inc.*, 134 IBLA 172 (1995), is misplaced. In that case, the IBLA found evidence of a market for *ungathered* gas at the wellhead in view of competing offers from independent purchasers. The gas in that case was produced at sufficient pressure and without impurities (such as $CO_2$ or $H_2S$) that would require treatment for removal. The circumstances of the rather unique *Xeno* case are not apposite here.

Nor is ARCO/Vastar's reliance on the Colorado Court of Appeals' decision in *Rogers v. Westerman Farm Co.*, 986 P.2d 967 (Colo. App. 1998), *cert. granted*, 1999 Colo. LEXIS 868, well founded. First, that case does not involve $CO_2$ removal. Second, regardless of whether the Colorado Supreme Court ultimately agrees that the dehydration costs in that case are deductible under the private lease instruments involved in that case, dehydration is a cost necessary to put production into marketable condition as a matter of law applicable to Federal leases. As the preamble to the current Federal gas valuation regulations observes, "post-production costs for the services of gathering, separation, measurement, dehydration, compression, and sweetening are considered to be a requirement to place lease production into marketable condition, at no cost to the lessor." 53 Fed. Reg. 1230, 1267 (Jan. 15, 1988). *See e.g., Texas Co.*, 64 I.D. 76 (1957); *Placid Oil Co.*, 70 I.D. 438 (1963); *R.E. Yarbrough & Co.*, 122 IBLA 217, 221 (1993).

*Conclusion*

Based on the record, and for the reasons stated herein, the petition for reconsideration is denied.

Because this decision is issued by an Assistant Secretary of the Department of the Interior, it is not subject to appeal to the Interior Board of Land Appeals and is the final action of

the Department. *Blue Star, Inc.*, 41 IBLA 333 (1979); *Marathon Oil Co.*, 108 IBLA 177 (1989).

Sincerely,

/s/ Piet deWitt
Piet deWitt
Acting Assistant Secretary,
Land and Minerals
Management

## APPENDIX E

[Seal Omitted]

United States Department of the Interior
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20240

September 12, 2000

**CERTIFIED MAIL**
**RETURN RECEIPT REQUESTED**

Mr. Charles A. Breer
Davis, Graham & Stubbs LLP
Attorneys at Law
370 17th Street - Suite 4700
P.O. Box 185
Denver, Colorado 80201-0185

Re: MMS-97-0155-O&G
Amoco Production Company

Appeal Denied in Part; Order Modified

Dear Mr. Breer:

Amoco Production Company (Amoco, the Appellant) appealed under 30 CFR Part 290 (1997) from the Mineral Management Service's (MMS) order dated May 27, 1997 (Order), directing Amoco to pay additional royalties of $4,117,607 and to perform a restructured accounting for all San Juan Basin Federal and Indian leases producing coalbed methane for the period January 1989 through August 1996, and to pay any additional royalties due.[1]

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[1] The audit period for the order to pay (January 1989-December 1996) differs from the period for the order to perform restructured accounting (January 1989-August 1996). Order at 1, 8. In addition, Amoco asserts that several of the "audited" leases are located in Colorado; even though the State's Issue Letter dated November 16,

The Order was based on an audit performed by the State of New Mexico in accordance with section 205 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. 1735 (1994). The New Mexico Taxation and Revenue Department (State) reviewed Amoco's royalty calculations[2] for coalbed methane produced from its Federal leases in the San Juan Basin.

Amoco's early coalbed gas sales occurred under conventional long-term gas contracts with El Paso Natural Gas Company (EPNG) at the wellhead, subject to EPNG's service fees for treating, gathering, compressing, transporting, and processing.[3] *See* Supplemental Statement of Reasons

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1995, limited the "audit" to "Federal leases in the San Juan 30-6 Unit located in Rio Arriba County, San Juan Basin, New Mexico." Issue Letter at 1. Two of the non-New Mexico audited leases purportedly are Southern Ute Tribal Leases Nos. 519-000033-0 and 519-000034-0. SOR at 1. Karen Anderson, representing the Southern Ute Tribe (Tribe), informed MMS that these two leases are part of the Tribe's audit of Amoco in Docket No. MMS-97-0190-IND. These are the only Tribal (and non-New Mexico) leases identified by Amoco. By letter dated December 9, 1998, MMS retracted these two leases from the Order's requirement to perform a "restructured accounting." Although it appears that MMS's action was adequate to allay Amoco's "audit" concerns, all Tribal leases nonetheless are hereby excluded from the May 27, 1997, order and from this appeal. Further, this decision does not address any Indian oil and gas interests of the regulations governing those interests, particularly the valuation regulations that were amended and recodified during the audit period. *See* 61 F.R. 5467 (February 12, 1996).

[2] For Amoco's leases in the Northeast Blanco Unit, the unit operator, Blackwood & Nichols Co., reported and paid royalties on Amoco's behalf.

[3] Some of these early contracts were between EPNG and Tenneco Oil Co. or Pan American. Amoco subsequently acquired these properties.

(SSOR) at Exhibit C, Mueller Affidavit at ¶¶ 29-33. These contracts typically contained release or spot sale provisions, which allowed Amoco to sell to alternate buyers either at the wellhead or at downstream locations. *Id.* Amoco and EPNG agreed to an amendment in late 1989 that superceded all prior sales contracts, and provided for gas sales at the tailgate of one or more gas treatment plants in the area.[4] *Id.* at ¶ 34.

During the audit period, Amoco's coalbed methane was treated for the removal of Carbon dioxide ($CO_2$) in three plants: Meridian Oil Gathering Inc.'s (MOGI) Val Verde Plant, Williams Field Services' (WFS) Ignacio Gas Processing Plant, and WFS's Milagro Treating Facility. With respect to methane, $CO_2$ has no energy content and reduces the energy value per unit of volume of the gas stream of which it is a part. $CO_2$ may also combine with water vapor in a gas stream to form carbonic acid ($H_2CO_3$). In some circumstances, $CO_2$ is recovered and is sold as a valuable product—for example, for use in crude oil enhanced recovery operations—but that is not the case here.

The coalbed methane transported to and treated at MOGI's Val Verde Plant was produced primarily from the San Juan 30-6 Unit, Agreement No. 891-000538-A, during the audit period. Field Report (FR) at 2. The $CO_2$ content of the gas entering the Val Verde Plant ranged from 10.8 percent in December 1988 to 12.2 percent in December in 1995. Order at 5. The cost of $CO_2$ removal is $0.0778 per Mcf. The

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[4] MOGI's Val Verde Plant and William Field Services' (WFS) Milagro Treating Facility are dedicated coalbed gas $CO_2$ removal plants. WFS's Ignacio Gas Processing Plant is a conventional gas processing plant used to separate liquefiable hydrocarbons from the natural gas stream as well as to remove $CO_2$.

transportation rate on the Val Verde "gathering system" to the plant is $0.3172 per Mcf from January 1989 through October 1990, and $0.2822 per Mcf from November 1990 through December 1996. *Id.* The gas leaves the Val Verde Plant and is marketed through EPNG's mainline transportation system. FR at 2.

The State audited Amoco's coalbed methane produced from the "30-8" Area and the Northeast Blanco Unit (NEBU), Agreement No. 892-000929-B, for the period May 1990 through December 1993. Order at 6; FR at 2. For the period February 1990 through June 1992, Amoco's production from those properties was processed in WFS's Ignacio Gas Processing Plant. Order at 6. The cost of services provided by WFS includes $0.1353 per Mcf for gathering, $0.0795 per Mcf for treating, and $0.0852 for transportation.[5] *Id.*

From July 1992 to December 1995, Amoco's coalbed methane entering the Mazanares System was treated in WFS's Milagro Treating Facility. *Id.* For NEBU production, the rates for WFS's gathering, treating, and transportation services based on Central Delivery Points (CDP's) are $0.26 for Simms Mesa CDP, and $0.30 for Pump Mesa

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[5] The "Gathering and Treating Letter Agreement" dated February 13, 1990, contemplated that production from the Northeast Blanco Unit and "30-8" Area would enter Northwest Pipeline Company's (NWPL) mainline at the tailgate of WFS's Ignacio Gas Processing Plant, but would ultimately be redelivered to EPNG's mainline. The "Discounted Coal Seam Gathering, Treating, and Transportation Rates and Purchase Obligation" dated June 15, 1990, is the apparent result of WFS's failure to complete the tie-in to EPNG's mainline by the specified date. The amendatory agreement provided for WFS/NWPL to purchase the "30-8" area and Northeast Blanco Unit production until the EPNG interconnect was completed.

and Middle Mesa CDP's. *Id.* Because some gas from the NEBU was processed in the Val Verde Plant during this period, the costs of services for that plant were used for that gas. *Id.* The production transported on the Manzanares System was purchased by either WFS or Northwest Pipeline Company (NWPL) and delivered to EPNG's mainline for transportation downstream of the treatment facilities. *Id.*

Based on MMS's April 22, 1996, Dear Operator/Payor Letter, the State determined that Amoco incorrectly calculated gross proceeds for the coalbed methane sales resulting in royalty deficiencies of $4,117,607. The deficiency assessment consists of: 1) $432,158 for San Juan 30-6 Unit production for this period January 1989 through December 1996; 2) $1,308,372 for Northeast Blanco Unit (NEBU) production for the period January 1990 through December 1995); 3) $2,170,962 for other than NEBU Manzanares System production for the period July 1992 through December 1995; and 4) $206,115 for other than San Juan 30-6 Unit Val Verde production for the period October 1992 through December 1995. The MMS issued Amoco an order to pay that amount (FBIL 26974005). Further, MMS deemed Amoco's deficient royalty accounting to be systemic for all of its leases in the San Juan Basin producing coalbed methane.

*Issues*

**I. Was $CO_2$ removal necessary to place the gas in marketable condition?**

**II. When coalbed gas is treated away from the lease, are the costs of transporting excess carbon dioxide ($CO_2$) deductible?**

**III. Does the April 22, 1996, Dear Operator/Payor Letter violate the Administrative Procedure Act?**

**IV. Can MMS collect royalties that become due more than six years before the date of the order to pay?**

I. *Analysis - Removal of $CO_2$ was Necessary to Put the Gas into Marketable Condition*

Amoco argues that the only requirement under the marketable condition regulation is for the lessee to place gas in the physical condition necessary to market it under contracts *typical for the field or area.* Statement of Reasons (SOR) at 6 (emphasis in original); Supplemental Statement of Reasons (SSOR) at 8. Amoco asserts that the lessee is not required to condition the gas, *i.e.*, remove $CO_2$, for "downstream markets." In support of its position, Amoco cites *Beartooth Oil and Gas Co. v. Lujan*, CV 92-99-BLG-RWA, 7, 4-5 (D. Mont. 1993) *opinion withdrawn after remand and settlement*; *Marathon Oil Co. v. United States*, 604 F. Supp. 1375, 1386 (D. Alaska 1985), *aff'd*, 807 F.2d 759 (9th Cir. 1986), *cert. denied*, 480 U.S. 940 (1987); *Independent Petroleum Ass'n of America v. Armstrong*, 91 F. Supp. 2d 117, 125 (D.D.C. 2000); *California Co v. Udall*, 296 F.2d 384, 387 (D.C. Cir. 1961); and *Xeno, Inc.*, 134 IBLA 172, 182 (1995). SOR at 7; SSOR at 9. On this basis, Amoco asserts that the untreated coalbed methane—before removal of the $CO_2$—was in marketable condition.

Amoco's citations are largely misplaced. Neither *Marathon* nor the recent district court decision in *IPAA* involved questions of putting gas into marketable condition. The question in *Marathon* was whether MMS had properly calculated Marathon's gross proceeds as the landed sales price in Japan of the gas in liquefied form less the costs of transportation (liquefaction and tankering). (The District of Alaska and the Ninth Circuit both answered in the affirmative.) The issues in *IPAA* involved primarily the lessee's duty to market at no cost to the lessor. Treatment of gas to put it in marketable condition was not involved. *California Co. v. Udall* involved gathering, compression, and dehydration necessary to put gas into marketable condition, and lends no support to Amoco's theory.

In *Xeno* and *Beartooth*, it was necessary to examine when gas was in marketable condition—and, consequently, whether certain costs incurred were necessary to put gas into marketable condition or were undertaken for other purposes. The Interior Board of Land Appeals (IBLA) in *Xeno* found that the gas produced under the particular circumstances of that case was in marketable condition at a point before where MMS said it was in marketable condition, but that was a fact-specific finding. It does not answer the question of whether Amoco's untreated coalbed methane was already in marketable condition at the point of extraction. To answer that question, we must examine the circumstances of the instant case more closely.

For the period January 1989 to October 1990, Amoco states that gas produced from certain wells was sold at arm's length to Burlington Resources Oil & Gas Company (formerly Meridian Oil, Inc.) at the wellhead. SOR at 3. Amoco claims that the gas was sold at the wellhead in marketable condition at the prevailing market price in the area. SOR at 8. Several examples of wellhead sales of untreated coalbed methane are presented in an affidavit from Ms. Cristina Sigdestad.[6] *See* SOR at Exhibit C, Sigdestad Affidavit at & 4.

On May 1, 1990, Amoco entered into a contract to sell virtually all of its coalbed gas at the wellhead to Amoco

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[6] Other wellhead sales are referenced in the Mueller affidavit. *See* SSOR at Exhibit C, Mueller Affidavit at ¶¶ 51-53, 55-57, 66-68. In addition, Amoco Energy Trading Co. (AETC) says it has over 50 third party contracts by which it purchases untreated coalbed gas at arm's length at the wellhead. *Id.* at ¶¶ 60-62. The Mueller affidavit also asserts that there is an active aggregator market at the wellhead. *Id.* at ¶¶ 63-65.

Energy Trading Co. (AETC).[7] *See* SSOR at Exhibit C, Mueller Affidavit at ¶ 39. The May 1990 contract provides for a price based on a calculated netback value. "AETC calculates the amount it owes Amoco by starting with the funds it receives from selling the gas to third parties,[8] and then subtracting any costs necessary to move the gas from the Delivery Point to the point where AETC sells the gas including costs to compress, dehydrate (away from the well), treat, and transport gas." The price calculation is similar to the manner in which Amoco determines value and pays MMS royalties. *Id.* at ¶ 41.

In further support of its argument that untreated coalbed gas is in marketable condition at the wellhead, Amoco provides affidavits[9] from Dr. Alfred L. Parker and Mr. Peter M. Mueller asserting that a significant and growing wellhead market exists for untreated coalbed gas in the San Juan Basin, and that the costs incurred downstream of the wells are for the purpose of enhancement of the gas for sale in secondary markets. SSOR at 4, 6-7.

In the Order, MMS asserts that the royalties paid on Amoco's coalbed methane production were based on a price that was reduced by the costs of gathering and treatment (primarily $CO_2$ removal). Order at 4, 7. The State calculated royalties for coalbed methane from the audited

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[7] Amoco sells to AETC, its corporate affiliate, approximately 307,000 MMBtu of untreated coalbed gas per day.

[8] In the mid-1990's, approximately two-thirds of AETC's gas was aggregated and sold in the San Juan Basin "pools." The remainder was sold downstream of the San Juan Basin pools. *See* SSOR at Exhibit C. Mueller Affidavit at ¶ 49.

[9] *See generally* SSOR at Exhibits B and C, Parker and Mueller Affidavits.

leases by applying the valuation regulations in 30 CFR Part 206 (1989) and the guidelines contained in MMS's Royalty Policy Board letter of December 7, 1995. The MMS Order reflected these calculations. This Order said:

> By letter dated December 19, 1995, the State requested Amoco to provide a breakdown of costs associated with transporting the coalbed methane to a processing plant. Amoco's response was based on information received from Meridian by letter dated May 29, 1996, that indicated a cost of the $CO_2$ removal to be $.0778 per MCF.

Order at 4.[10]

The so-called "marketable condition rule" in the Federal gas valuation regulations provides:

> The lessee is required to place gas in marketable condition at no cost to the Federal Government or Indian lessor unless otherwise provided in the lease agreement. Where the value established pursuant to this section is determined by a lessee's gross proceeds, that value shall be increased to the extent that gross proceeds have been reduced because the purchaser, or any other person, is providing certain services the cost of which ordinarily is the responsibility of the lessee to place the gas in marketable condition.

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[10] The State's royalty calculations are far more complicated than the quoted passage implies due to multiple dispositions of coalbed methane production from the San Juan Basin. The costs of gathering and transportation are provided for the Val Verde and Manzanares Systems and the costs for treatment are provided for the Val Verde, Ignacio, and Milagro facilities. *See* Order at 5-7.

30 CFR 206.152(i) (1989).

Further, the regulations define marketable condition as "lease products which are sufficiently free from impurities and otherwise in a condition that they will be accepted by a purchaser under a sales contract typical for the field or area." 30 CFR 206.151 (1989).

The "marketable condition" rule has been uniformly upheld, and the lessee's obligation to put production into marketable condition at no cost to the lessor is uncontested. *E.g., Mesa Operating Limited Partnership v. Department of the Interior*, 931 F.2d 318 (5th Cir. 1991), *cert. denied*, 502 U.S. 1058 (1992); *California Co. v. Udall*, 296 F.2d 384 (D.C. Cir. 1961).

Whether untreated gas was sold under a contract that is typical for the field or area from which it is produced is pertinent to the valuation issue here. The demand for wellhead sales of untreated San Juan Basin coalbed gas that is utilized in that form is very limited and is not by any means the "typical" sales arrangement for that gas. Based on the volumes of each type of sale in the San Juan Basin, the dominant market for gas from the area is for the gas that is utilized in distant markets with a much lower $CO_2$ content.[11] As Amoco admits, "[A]lthough there is a market

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[11] Excluding seasonal variations, Amoco documents a maximum of approximately 105 MMcfd of untreated coalbed methane sold at the wellhead and used by various entities in that form. Mueller Affidavit at ¶¶ 51-59, 66-68. Based on Burlington Resources Oil and Gas Company's (formerly Meridian Oil Inc.) and ARCO/Vastar's sales and purchases from the San Juan Basin, a maximum of approximately 60 MMcfd is untreated coalbed methane that is sold at the wellhead and utilized in that form. Together, these uses of untreated coalbed methane represent approximately 10 percent of total San Juan Basin coalbed methane production. Summation of figures found at page 2

for unprocessed coalbed gas at the well, *that wellhead demand is limited due to the lack of industrial and residential users in the San Juan Basin.* Consequently, much of the gas must be transported to distant users, . . ." SOR at 4 (emphasis added). Moreover, Amoco does not establish—and, indeed, does not even assert—that industrial and residential users could use untreated high-$CO_2$ content gas. Furthermore, although Amoco asserts that there could be an active end-user market for gas with $CO_2$ content great than 10 percent, such a market does not exist.

With the submittal of its SSOR, Amoco attempts to retreat from some of the statements it made. Amoco's arguments in its SSOR do not refer to what it previously (and correctly) characterized as a "limited" wellhead market for untreated coalbed gas. Amoco now talks in terms of a supposedly extensive and viable wellhead market. SSOR at 4. Further, the SSOR is supplemented with the assertions contained in the Parker and Mueller Affidavits.

The question requiring resolution is whether the production sold at the wellhead is in marketable condition prior to its subsequent treatment and transportation for use in distant markets. In other words, is the market at the wellhead the primary market for the gas as opposed to the more distant market?

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of ARCO/Vastar's SSOR for MMS-97-0063-O&G (quoting Larry Anderson, "San Juan Basin Coalbed Gas Unique Regional Transportation Facilities" at 3.) and page 2 of the Edlund Affidavit of ARCO/Vastar's SSOR. *Atlantic Richfield Co.*, MMS-97-0063-O&G, MMS-97-0191-O&G (2000), 22 Gower Federal Service, Royalty Valuation and Management, Rocky Mtn. Min. L. Found. *Cf. infra* notes 17, 23.

Not only has the Department previously addressed the issue of removing only $CO_2$ in the marketable condition context,[12] the issue of acid gas removal has also been addressed.[13] In *Exxon*, IBLA stated that "it cannot be said that the transfer of title to the sour gas while it was still in its untreated condition meant that appellants were marketing untreated gas. . . . the fact that appellants bore the costs of sweetening meant that they were effectively marketing sweetened gas." *Exxon, U.S.A.*, 121 IBLA 234, 248-49 (1991).[14]

Here, two facts remain uncontroverted. One, the wellhead market for gas in an untreated condition is a limited "market" that is separate and distinct from the wellhead market for gas that is further treated; and two, Amoco is effectively marketing sweet gas by paying for the costs of treatment through a contractual pricing mechanism with AETC. Under these circumstances, IBLA's conclusion in *Texaco* that the value of production for royalty purposes cannot be reduced by the costs of sweetening applies.[15]

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[12] *See Atlantic Richfield Co.*, MMS-97-0063-O&G, MMS-97-0191-O&G (2000), 22 Gower Federal Service, Royalty Valuation and Management, Rocky Mtn. Min. L. Found.

[13] *See Exxon Company U.S.A.*, 121 IBLA 234 (1991); *Apache Corp.*, 127 IBLA 125 (1993); *Texaco, Inc.*, Civ. No. 96-CV-08-J (D. Wyo. April 9, 1997).

[14] *See also Apache Corp.*, 127 IBLA 125, 134 (1993) (reducing royalty value by sweetening costs would amount to a subsidy by the Government equal to the royalty rate times those costs); *Texaco, Inc.*, Civ. No. 96-CV-08-J, slip op. at 5 (D. Wyo. April 9, 1997) (there is no market for sour gas if the seller pays to treat the gas, even though the purchaser accepts the gas untreated).

[15] "CIG's willingness to purchase Texaco's sour gas for a price which includes a reduction for CIG's costs of removing the hydrogen

Purchasers of gas from the field or area generally demand that the gas be properly conditioned for sale in the actual markets, which requires a lower $CO_2$ content. The fact that some purchasers are willing to purchase gas before conditioning and perform the conditioning themselves does not alter the finding that the gas requires conditioning. This is particularly true where the typical contracts for sales of gas from the field or area are in line with general national standards.[16] The Department of the Interior cannot allow producers simply to alter the form of their sales arrangements in order to force the lessor to share in the producers' costs to place the product in marketable condition.

Further, Amoco's contention that the treatment of coalbed gas constitutes enhancement of the gas has no merit. This simply an argument against the marketable condition rule and is contrary to established law.

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sulfide from the gas does not establish that the sour gas was in marketable condition when it was sold to CIG or that the reduced price constitutes the reasonable market value of the production." *Texaco, Inc.*, 134 IBLA 109, 115 (1995).

[16] Amoco argues that its non-arm's-length sales of untreated coalbed gas to AETC are typical for the field. However, the coalbed gas in its natural wellhead state was never intended to be "marketed" but only sold on that basis. *See California Co.*, 296 F.2d at 388 (indicating the clear difference between marketing and selling). The market demand for the product is overwhelmingly conditioned gas free from excess $CO_2$. Thus, the predominant actual "market" consists of purchasers buying gas in a treated condition, not the artificial market created by resellers to avoid production-related costs of placing the gas in a marketable condition. The artificial nature of the purported market for untreated gas is obvious. Without the downstream market for treated gas, the sales of untreated gas would not have occurred due to lack of demand.

Here, there was limited demand for the product in the condition in which it was extracted at the wellhead. Consequently, the value for royalty purposes must be determined by adding to the gross proceeds received from the wellhead purchaser the cost of treating the gas for the removal of $CO_2$ to the level required to place the gas in marketable condition. Thus, the portion of the appeal claiming that the gas is in a marketable condition at the time of sale at the wellhead is denied.

Amoco also argues that MMS's requirement to condition the gas to an interstate pipeline standard of two percent (2%) $CO_2$ content is arbitrary and contrary to law. SOR at 8-11. In *California Co. v. Udall, supra*, the quality standard that established the marketable condition of the production was the standard required by the receiving pipeline because the wellhead gas sales contract specifically required the pipeline standard for production quality. Here, the gas must first meet the pipeline standard of quality before shipment to the market because the predominant market is not in the field or area. Therefore, transporting the production to a market outside the field or area is necessary to market the gas.

As discussed above, there is only a very limited use or sales of the gas in its wellhead condition. For a market to exist, there must be "an established demand for an identified product." *California Co. v. Udall*, 296 F.2d at 388. There is no evidence that a market exists for gas unless is it conditioned to meet the mainline specifications. Thus, the minimum required condition of the coalbed methane for marketing (and royalty) purposes is the quality required to supply the market(s) where the demand exists.

The MMS's regulations define marketable condition in terms of the quality requirements of a typical sales contract for the field or area.[17] 30 CFR 206.151. The mainline quality requirements are reflective of the required condition of the gas for sales of production from the field or area. If the production does not meet mainline specifications for transport to the downstream interconnect or end use, the production is effectively unusable. Accordingly, I find that the mainline transporters' $CO_2$ quality requirements

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[17] Amoco's figures indicate that if all sources using Amoco's untreated coalbed gas were at maximum utilization (not factoring seasonal variations), they would comprise approximately 15.59 percent of Amoco's produced coalbed gas. Percentages derived from figures contained in Exhibit B, Mueller Affidavit at ¶¶ 51-59, 66-68. In *Atlantic Richfield Co.*, the record indicated that Burlington's and ARCO/Vastar's use, or sale of others' use, of untreated coalbed methane constituted less than 10 percent of the total coalbed methane entering the Val Verde Plant. Both *Atlantic Richfield Co.*, MMS-97-063-O&G, MMS-97-0191-O&G (2000), and the instant case concern the same field and area, the San Juan Basin during the same period (1989-1996). The percentages identified above the untreated coalbed methane used in that form in the field and area includes uses, or sales for others' uses, by Amoco, Vastar, and Burlington. Together these companies produce a substantial amount of the coalbed methane from the San Juan Basin. *See* RIK volumes volunteered in the companies' August 7, 1995, Royalty-in-Kind Onshore Pilot Program Agreement. Assuming *arguendo*, that the other San Juan Basin major producers' utilization, or sale of others' utilization, of untreated coalbed methane is marginally greater than that described above, the use of untreated coalbed methane would still not equal 20 percent of the total San Juan Basin coalbed methane produced. Thus, the sale of coalbed methane at the wellhead that is utilized in an untreated form does not constitute the "typical" sale of coalbed methane in the San Juan Basin.

effectively establish a marketable condition standard for gas sold from the field or area.

Based on the analysis above, this portion of the appeal is denied. However, the mainline quality standard (2% $CO_2$) used by the State in computing royalties does not agree with the mainline quality standards identified for the field and area for portions of the audit period (1 - 3% $CO_2$). The "Gathering and Treating Letter Agreement" dated February 13, 1990, states that "Williams shall provide sufficient treating to meet current EPNG specifications of one percent (1%) carbon dioxide." Letter Agreement at ¶ A. Although the quality of treatment required by EPNG is one percent (1%) $CO_2$ content, the gas that is sold to WFS/NWPL is transported in the NWPL mainline which specifies a three percent (3%) $CO_2$ content requirement. *See* NWPL tariff, Exhibit B to Letter Agreement. *See also Atlantic Richfield Co.*, MMS-97-0063-O&G, MMS-97-0191-O&G, (2000), 22 Gower Federal Service, note 10 (indicating evidence of different pipeline standards ranging from 1% - 3% of $CO_2$ content for the San Juan Basin field or area during the audit period).

Therefore, the Order is modified and the Appellant must recalculate the royalties due for the audited leases during the audit period based on the $CO_2$ content acceptable to the pipeline purchasers. The lessor will not share in treatment costs simply because one purchaser may require a marginally lower $CO_2$ content than another. Nor will the lessor require the lessee to condition the gas to a higher level of purity than the pipeline purchaser requires.

*Summary*

To summarize this section, the costs of removing $CO_2$ are the responsibility of the lessee when gas must be conditioned to meet the quality requirements typical for sales of gas from the field or area. Where there is no market for gas in the field or area, the marketable condition require-

ment is the quality of the mainline transportation to the downstream market. The actual mainline quality specifications shall be used in all instances, including any quality specifications that were "grandfathered." Thus, this portion of the appeal is denied and the Order is modified as explained above.

II. *Analysis - Amoco May Not Claim an Allowance for the Costs of Transporting $CO_2$ in Excess of Pipeline Specified Levels*

a. *Wellhead/CDP to Plant*

The MMS states in the Order that "[t]ransportation allowances are granted for the reasonable, actual necessary costs of transporting the coalbed methane from the royalty measurement point (either the well or the Central Delivery Point (CDP) [)] to the point of sale remote from the lease." Order at 2. Further, "no allowance may be taken for the costs of transporting lease production which is not royalty bearing without MMS approval." 30 CFR 206.157(a)(2)(i) (1989).

The transporters at or near the tailgates of the three $CO_2$ removal plants (*e.g.*, EPNG, NWPL, and Transwestern Pipeline Company) specify in their transportation agreements that the gas quality cannot exceed from one to three percent of $CO_2$ for mainline transport.[18] In addition, the

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[18] "The record indicates that the mainline transporters' (El Paso Natural Gas, Transwestern, and Northwest Pipeline) $CO_2$ quality requirements vary from one to three percent (1-3%) content of coalbed methane volume over the audit period. SSOR at Exhibit No. 5. Further, El Paso Natural Gas 'grandfathered' the $CO_2$ allowed for mainline transportation from the Val Verde Plant at 2.13 percent. *Id.* (*see* Tariff No. 221 dated July 7, 1994)." *See Atlantic Richfield Co.*, MMS-97-0063-O&G, MMS-97-0191-O&G at 7, n. 10 (and accom-

guidance provided by MMS states that "transportation costs [can only be] allocated to the methane component for the amount of $CO_2$ permitted in the main (inter- or intrastate) transmission line." Dear Operator/Payor Letter at 2. Consequently, the State disallowed costs to transport $CO_2$ exceeding two percent (2%) of the combined volume of gas. Order at Schedules C, D, E, and F.[19]

Amoco argues that the State is restricting the allocation of transportation costs to gas that is at the interstate pipeline standard, and that the State considers $CO_2$ in excess of that standard a non-royalty bearing product. SOR at 12. Amoco contends that the cost of removing $CO_2$ should be included as part of the transportation allowance because unmarketable $CO_2$ is a waste product to which no allocation of transportation costs should apply in accordance with 30 CFR 206.157 (a) (2) (i) (1989). SOR at 12-14.

Further, Amoco states that the primary reason for removing the $CO_2$ is to transport the gas stream, not to place it in marketable condition. SOR at 14-15; SSOR at 7, 10, 12-13. Amoco avers that removal of the $CO_2$ enhances the value of the production for downstream sales. Consequently, Amoco believes that an allowance for the cost of enhancement should be available as a deduction from the downstream

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panying text). For the instant case, the producing basin, the mainline transporters and the audit period are virtually the same.

[19] There is no explanation why two percent $CO_2$ content is used for royalty purposes rather than the specified requirements of one percent (1%) $CO_2$ content for EPNG as recognized in the Gathering and Treating Letter Agreement. Letter Agreement at 1. Also, Article 14 of the Gathering and Treating Letter Agreement provides for Amoco to deliver coal seam gas at NWPL's quality specifications (3% $CO_2$). *See* Letter Agreement at Exhibit B, § 3.1(c).

value of the gas for royalty purposes. SSOR at 3, 10, 12-13. Amoco concludes that $CO_2$ removal should be treated the same as the dehydration costs in *Exxon*, 118 IBLA 221, 240, 250, and the liquefaction costs in *Marathon Oil Co. v. United States*, 604 F. Supp. at 1375, 1381-86 (D. Alaska 1985), *aff'd*, 807 F.2d 759 (9th Cir. 1986), *cert. denied*, 480 U.S. 940 (1987), and because of its enhancement capacity, should not be subject to royalty as detailed in *Xeno, Inc.*, 134 IBLA at 180, 183-84, and *IPAA*, 91 F. Supp. 2d at 120, 125. SOR at 14-15; SSOR at 3, 9-13. I disagree with the Appellant's contentions.

For the audit period, the record is unclear regarding whether all of Amoco's gas was sold at the wellhead.[20] When

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[20] The only sales agreement included in the record is the Discounted Coal Seam Gathering, Treating, and Transportation Rates and Purchase Obligation dated June 15, 1990. This agreement provides only for the temporary purchase of the "30-8" and Sims Mesa area production (also known as Ignacio Plant volume reduction) until such time that the WFS Interconnect is completed with the EPNG mainline. Also, Amoco alludes to an arm's-length wellhead sale to the Burlington Resources Oil and Gas Company (formerly Meridian Oil, Inc.) for the period January 1989 through October 1990. However, Amoco's SSOR contains descriptions of Amoco's wellhead sales contracts (2) with Burlington Resources and Amoco's wellhead purchase contracts (54) with various third parties, as well as descriptions of numerous wellhead sales contracts between various parties in the San Juan Basin. SSOR at Parker Affidavit, Exhibits ALP-8 and ALP-10. Prior to 1989, most of Amoco's San Juan Basin production was sold at the wellhead to El Paso Natural Gas Pipeline. SSOR at Exhibit B, Mueller Affidavit at ¶¶ 29-34. Commencing in 1990, Amoco sold virtually all of its coalbed gas that is produces form the San Juan Basin to AETC at the wellhead. Id. at ¶¶ 39-41. Amoco's other wellhead dispositions of coalbed gas are also discussed. Id. at ¶¶ 48-68.

valuing production that is sold at arm's length at the wellhead under 30 CFR Part 206, the cost of transportation downstream of the wellhead is not a factor and there is no transportation allowance.

The State argues that since a rate per Mcf is charged AETC for transporting the entire coalbed gas stream, the portion of the fee applicable to the $CO_2$ content in excess of the mainline allowable cannot be ignored for royalty purposes. Therefore, because payments to Amoco for gas sales under Unit Operating Agreements/Joint Operating Agreements or any other contract at the wellhead/CDP reflects a reduction for the costs of gathering, treating, and transporting the coalbed methane, those costs must be added back into the payment received by Amoco to determine the value of production for royalty purposes.

When coalbed methane is sold arm's length at the wellhead, the cost of transportation downstream of the point of sale would not be deducted separately as an allowance under 30 CFR 206.156 and 206.157 (1989). Similarly, for all production sold at the wellhead of CDP's for the remainder of the audit period, there is no transportation allowance for royalty valuation purposes. The addition of the costs of transporting the $CO_2$ component above the mainline standards to the lessee's wellhead gross proceeds is warranted in this situation because to do otherwise would have the lessor share in costs that it would not otherwise share in simply by the vehicle chosen by the lessee in selling its production.[21]

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[21] Amoco receives a price for gas from AETC that is AETC's arm's-length proceeds from third parties net of costs of gathering, treating, and transporting the gas to the point of sale. *See* SSOR at Exhibit C, Mueller Affidavit at ¶ 41. The State argues that the net price received by Amoco must be adjusted by adding back in all costs

Amoco misconstrues the decision in *IPAA* in arguing that the removal of $CO_2$ is an enhancement process for the sale of production in secondary markets. As determined in Section I, above, the removal of $CO_2$ is necessary to put production into marketable condition. Thus, the conclusion in *IPAA* that MMS does not have "the authority to define value to include downstream costs unrelated to production of the gas" does not apply here.[22]

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associated with placing the gas in marketable condition (*e.g.*, costs of gathering and treat the coalbed gas), and transportation of $CO_2$ in excess of the mainline allowable. Thus, the State perceives the valuation issue to be one in which the lessee has failed to place the gas in a marketable condition at no cost to the lessor. In the instant case, AETC (the purchaser), assuming the lessee's marketable condition duty, is a wholly-commonly-owned affiliate of the lessee. If the proceeds received by the wholly-commonly-owned affiliate minus applicable transportation costs (not including excess $CO_2$ transportation) were used for royalty valuation purposes, the result presumably would be the same as that now sought by the State given the AETC/Amoco pricing arrangement described above. However, the State did not examine AETC's resale proceeds, and we therefore, do not address the issue of the wholly-commonly-owned affiliate's resale proceeds in this decision.

[22] *See IPAA*, 91 F. Supp. 2d at 125.

The fact that a producer can sell relatively small volumes[23] of coalbed gas in an untreated condition does not make the gas, most of which must be treated for downstream sale, marketable in an untreated condition. The decision in *IPAA* did not address costs necessary to put production into marketable condition and did not affect the non-deductibility of those costs.

b. *Post-Plant Sales*

For all gas that is sold downstream of the wellhead or CDP, a transportation allowance may be applicable. However, evidence of the post-treatment selling arrangements is not contained in the record. For any of these sales of coalbed methane that occur, the regulations at 30 CFR 206.156 and 206.157 (1989) govern applicable transportation allowances, subject to the determination in II.c. below.

c. *Transportation of Waste*

Amoco argues that the State incorrectly computes the allowable costs of $CO_2$ transportation both from the wellhead/CDP to the plant and from the plant to the point of

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[23] Amoco's figures indicate that if all sources using Amoco's untreated coalbed gas were at maximum utilization (not factoring seasonal variations), they would comprise approximately 15.59 percent of Amoco's produced coalbed gas. Percentages derived from figures in Exhibit B, Mueller Affidavit at ¶¶ 51-59, 66-68. However, in accordance with the State's analysis, "less than one tenth of one percent of the *total* coalseam production . . . is sold and truly valued with the carbon dioxide entrained in the gas stream." State's Response to Amoco's SSOR at 4. Six treatment plants in the San Juan Basin typically treat coalbed methane gas, Val Verde, Milagro, Arkansas Loop, Florida River, La Maquina, and Esparanza. MMS October 1995, "Coalbed Methane Royalty Issues." However, coalbed methane may also flow to and through or bypass other plants in the San Juan Basin, *e.g.*, Blanco, San Juan, and Ignacio.

sale. Amoco contends that allocation to the methane stream of the costs of transporting a $CO_2$ waste product comports with the valuation regulations and that there is no reason for treating amounts of "waste" $CO_2$ within interstate pipeline standards, i.e., less than two percent, differently than amounts in excess of those standards. Finally, Amoco argues that is arbitrary for MMS to allow a deduction for two percent of $CO_2$ content, but not for the amount of $CO_2$ content at issue here. SOR at 12-14. I disagree.

The issue of transporting $CO_2$ in excess of the mainline quality standard downstream of the plants has already been addressed, in effect, by the marketable condition determination in section I. above. In other words, because the coalbed methane must be placed in a marketable condition prior to mainline transport, there are no $CO_2$ volumes that must otherwise be transported downstream of the plant. Thus, the sole issue regarding $CO_2$ waste volumes pertains to the transportation of the coalbed methane from the wellhead/CDP to the processing/treatment plants.

The guidance by the *Payor Handbook* notes that "[t]ransportation costs for a gaseous stream [or a liquid and gaseous stream] are allocated only to the royalty-bearing and non-royalty-bearing products. For transportation cost allocation purposes, a waste product is considered neither royalty-bearing nor non-royalty bearing. Therefore, the waste product volume is excluded from the cost allocation." *Payor Handbook* 6.4.1.

The three examples contained in section 6.4 of the *Payor Handbook* all assume that $CO_2$ is a waste product. Additional guidance is contained in the April 22, 1996, Dear Operator/Payor Letter. In assessing additional royalties on Amoco for transportation of $CO_2$ volumes, MMS followed the guidance in the Dear Operator/Payor Letter, which states:

> For coalbed methane production, you can increase the transportation costs allocated to the methane component for the amount of $CO_2$ permitted in the main (inter- or intrastate) transmission line. For example, if your gas stream consists of 90 percent methane and 10 percent $CO_2$ and the main transmission line allows 2 percent $CO_2$ in the makeup of its gas stream you can include the costs of transporting the 2 percent $CO_2$ volume (or 92 percent of the total transportation cost) when calculating your allowance for methane.

Dear Operator/Payor Letter at 2.[24]

The valuation regulations address waste as follows:

> [T]he total transportation costs shall be allocated in a consistent and equitable manner to each of the products transported in the same proportion as the ratio of the volume of each product (excluding waste products which have no value) to the volume of all products in gaseous phase (excluding waste products which have no value). Except as provided in this paragraph, no allowance may be taken for costs of transporting lease production which is not royalty bearing.

30 CFR 206.157 (a) (2) (i); 206.157 (b) (3) (i).

The preamble to the revised valuation regulations published in the *Federal Register* on January 15, 1988, provides:

> The MMS does not agree with the commenter's proposal that the cost of the transporting nonroyalty-

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[24] A Dear Payor Letter issued February 4, 1988, also addresses transportation cost allocation among products, but it does not contain the $CO_2$ instructions issued in the April 22, 1996, Dear Operator/Payor Letter.

> bearing substances should be shared by the lessor in all instances. However, upon review, MMS has recognized that it is appropriate to provide an allowance which includes the costs of transporting certain non-royalty-bearing substances such as waste products, including water. For example, there may be circumstances where transportation of water along with the royalty-bearing portion of the production is necessary. For other than waste products, the final rule provides, however, that prior MMS approval is required before an allowance may be taken for the costs of transporting non-royalty-bearing substances.

53 F.R. 1230, 1258 (1988).

The regulations do not specifically explain the distinction between "non-royalty-bearing products" and "waste products." The guidance provided in the Dear Operator/Payor Letter treats $CO_2$ as a non-royalty-bearing product, but then directs the operator/payor to "use the regulation in 30 CFR 206.156 and 206.157 (1995) and the instructions in Chapter 6 of the *Oil and Gas Payor Handbook*, Volume III, to calculate your transportation allowance."

Arguably, one could infer from the *Payor Handbook* hypotheticals that $CO_2$ in this situation is assumed to be a "waste product." To do so, however, would be incorrect.[25]

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[25] The Payor Handbook examples at 6.4.1, 6.4.2, and 6.4.3, contain unfortunate ambiguities. They refer to gas streams that have MMBtu measures of $CO_2$ and helium. Neither $CO_2$ nor helium have energy contents (Btu's). Thus, the hypothetical examples are difficult to apply because we have no idea of the volumes of these gas stream constituents upon which to compute transportation allowances.

The intent of the *Payor Handbook* examples is apparent. Proportionate measures of the identified gas stream constituents affect the computation of transportation allowances. Had the numbers given in the examples represented volumes instead of Btu's, the results would have been what MMS intended. Then, the reference to $CO_2$ as a waste product would have made sense with respect to the regulations.

The MMS allocates the cost of transporting the mainline allowance non-methane constituents in a gas stream to the methane component. This is the only portion of non-royalty-bearing production that is considered a waste product. Even if the *Payor Handbook* examples, the fraction of $CO_2$ in the examples represented typical mainline allowables; representing from one to two-and-one-half percent (1-2½%) of the heating value (sic) of the gas stream.

The Dear Operator/Payor Letter guidance primarily treats the $CO_2$ content that was removed from the coalbed methane as a non-royalty-bearing product. Only the pipeline allowable $CO_2$ content (remaining in the methane stream) is treated as a waste product.[26] Beyond a point, pipeline tolerances[27] dictate against further removal of impurities, which then become a waste product (as opposed to its non-royalty-bearing status if present in amounts greater than the quality specifications of the mainline).

The valuation regulations specify that transportation costs are to be allocated to all royalty-bearing products after ex-

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[26] The cost to transport the interstate pipeline allowable $CO_2$ content is allocated to the methane and allowed as a cost of transporting the methane. *See* Dear Operator/Payor Letter at 2.

[27] Pipeline tolerance used in this context refer to the physical ability of the pipeline to operate efficiently at certain levels of non-methane constituents or contaminants.

cluding waste products, both from the total volume and from the volume of all products. 30 CFR 206.157 (a) (2) (i); 206.157 (b) (3) (i). In addition, the preamble providing the rationale for these regulations clearly indicates that the cost to transport non-royalty-bearing products that are not waste products will not be included in the allowable transportation deduction for royalty-bearing products. 53 F.R. 1230, 1258 (1988). The preamble implication that MMS will approve an allowance for the costs to transport non-royalty-bearing substances is limited to those non-royalty-bearing substances that are also waste products as defined above. *Id.*

Here, the $CO_2$ produced in conjunction with the methane from the coalbed is transported to a processing/treatment plant, separated (save for approximately two percent content) from the methane, and vented. There is no market for this $CO_2$. The intent of MMS's regulations and *Payor Handbook* is that waste production for the purpose of determining allowable transportation costs is the fraction of non-royalty-bearing production that is allowable in a mainline transportation system. In the instant case, all $CO_2$ in excess of the mainline standard is non-royalty-bearing production. Therefore, this portion of the appeal is denied.

Consistent with the modification in section I. above, the mainline standard of allowable $CO_2$ (2% $CO_2$) used by the State in computing royalties does not agree with the mainline quality standards identified in the record for portions of the audit period (1-3% $CO_2$).[28] Therefore, the Order is modified and the Appellant must recalculate the royalties

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[28] *See supra* note 18.

due for the audited leases during the audit period based on the guidance above.

III. *Analysis - The April 22, 1996, Dear Operator/Payor Letter Does Not Violate the Administrative Procedure Act*

Amoco avers that the State is applying the April 22, 1996, Dear Operator/Payor Letter as a rule in violation of the Administrative Procedure Act (APA). 5 U.S.C. 551-559, 701-706 (1994). In support of its position, the Appellant cites *Phillips Petroleum Co. v. Johnson*, 22 F.3d 616 (5th Cir. 1994), *modified on other grounds*, 1994 WL 484506, *cert. denied*, 514 U.S. 1092 (1995). Under *Phillips*, the court determined that APA required notice and comment rulemaking for the valuation procedures at issue in that case. In addition, Amoco argues that the supposedly newly instituted procedures cannot be applied retroactively. SOR at 16.

Here, the State applied the existing valuation regulations which were further explained by the April 22, 1996, Dear Operator/Payor Letter. To the extent that the State's interpretation was inconsistent with the regulations, this decision modifies the Order to make it consistent with the regulations.

When, through notices of interpretive rules, the Government explains and clarifies existing regulations, the procedural requirements of formal rulemaking under the Administrative Procedure Act, 5 U.S.C. 553 (1982), are not applicable. *Venlease I*, 99 IBLA 387 (1987). *See Shalala v. Guernsey Memorial Hospital*, 514 U.S. 87, 115 S.Ct. 1232 (1995). The Dear Operator/Payor Letter is an interpretation of existing regulations. Therefore, this portion of the appeal is denied.

IV. *Analysis – The Statutory Bar is Inapplicable to Administrative Appeals*

Amoco argues that any part of MMS's demand seeking royalties that accrued more than six years prior to the

demand is barred by the six-year statute of limitations in accordance with 28 U.S.C. 2415 (1994). However, rather than develop an argument on this issue, Amoco preserved this issue for use on the event of a further appeal. SOR at 16-17.

This proceeding is an administrative appeal and the statutory bar is inapplicable. *Foote Mineral Co.*, 34 IBLA 285, 306 (1978); *Anadarko Petroleum Corp.*, 122 IBLA 141 (1992). Therefore, the Appellant's claims with respect to the statute of limitations are without merit and this portion of the appeal is denied.

*Conclusion*

**I. Was the cost of $CO_2$ removal necessary to place the gas in marketable condition?**

The gas was not in marketable condition for its object market. The cost to place the production into marketable condition is to be borne by the lessee at no cost to the lessor. Thus, the proceeds received at the wellhead/CDP for gas must be increased by the cost of placing the gas in marketable condition. The removal of $CO_2$ from the coalbed gas stream is required to place the gas in marketable condition. Costs to place gas in marketable condition do not qualify as costs of processing.

**II. When coalbed is treated away from the lease, are the costs of transporting excess carbon dioxide ($CO_2$) deductible?**

When the gas is sold at the wellhead, no transportation costs are allowed to be deducted from the value of production for royalty purposes. Costs to transport non-royalty-bearing production to enable the production to be placed in a marketable condition are not allowed, except to the extent that the mainline transporter allows a specified amount.

When the lessee transports gas from the lease to a point of sale away from the lease, the cost to transport the gas may

be allowable. The cost to transport gas is not allocable to waste products, but is allocable to royalty-bearing and non-royalty-bearing, non-waste production. The portion of the cost allocated to non-royalty-bearing products is not deductible as an allowance. Waste is defined as the mainline allowable portion of a particular non-methane constituent of the gas.

**III. Does the April 22, 1996, Dear Operator/Payor Letter violate the Administrative Procedure Act?**

The Dear Operator/Payor Letter is an interpretive guide to existing regulations. Thus, the procedure contained in the Dear Operator/Payor Letter does not violate the Administrative Procedure Act.

**IV. Can MMS collect royalties that are more than six years past due?**

Because the statutory bar is inapplicable to administrative appeals, 28 U.S.C. 2415 has not been violated.

Amoco must recalculate the royalties due accordingly.

Because this decision is issued by an Assistant Secretary of the Department of the Interior, it is not subject to appeal to the Interior Board of Land Appeals and is the final action of the Department. *Blue Star, Inc.*, 41 IBLA 333 (1979); *Marathon Oil Co.*, 108 IBLA 177 (1989).

/s/ Sylvia V. Baca
Sylvia V. Baca
Assistant Secretary, Land
and Minerals Management

Enclosure

**APPENDIX F**

[Seal Omitted]

# United States Department of the Interior

**OFFICE OF THE SECRETARY**

**WASHINGTON, D.C. 20240**

March 24, 2000

CERTIFIED MAIL
RETURN RECEIPT REQUESTED

Ms. Norma J. Rosner
Associate General Counsel
Vastar Resources, Inc.
15375 Memorial Drive
Houston, Texas 77079

Re: MMS-97-0063-O&G
MMS-97-0191-O&G
Atlantic Richfield Company
Vastar Resources, Inc.

Appeal Denied in Part;
Order Modified

Dear Ms. Rosner:

Atlantic Richfield Company (ARCO/Vastar, the Appellant)[1] appealed under 30 CFR Part 290 (1997) from the Minerals Management Service's (MMS) order dated January 22, 1997 (Order), directing ARCO/Vastar to pay additional royalties of $782,373 and to perform a restructured accounting for all San Juan Basin Federal and Indian leases producing coalbed methane that is transported and processed through the Val Verde System for the period January 1989 through August 1996 (audit period), and to pay any

[1] The January 22, 1997, Order relates to properties that were assigned by ARCO to its subsidiary, Vastar Resources, Inc. (Vastar). However, since the Order may affect other property and interests retained by ARCO, ARCO and Vastar are jointly responding to the Order.

additional royalties due.[2] ARCO/Vastar's appeal of the Order was assigned docket No. MMS-97-0063-O&G. ARCO/Vastar also appealed an MMS. Royalty Valuation Division (RVD), decision dated July 14, 1997 (RVD Decision), concerning some of the same leases and issues as the Order. The MMS assigned docket No. MMS-97-0191-O&G to ARCO/Vastar's appeal of the RVD Decision.

The Order was based on an audit performed by the State of New Mexico in accordance with section 205 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. 1735 (1994). The New Mexico Taxation and Revenue Department (State) reviewed ARCO's royalty calculations for coalbed methane produced from its leases in the San Juan No. 30-6 Unit (audited leases).[3] Prior to April 1992, the coalbed methane produced from this unit was sold arm's-length at the wellhead before it was transported through Meridian Oil Gathering Inc.'s (MOGI) Val Verde System to the Val Verde Plant for removal of carbon dioxide ($CO_2$). Although the production continued to be treated in the Val Verde Plant after March 1992, the gas was sold under various selling arrangements downstream of the plant.

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[2] The restructured accounting order provides that all Federal and Indian leases must be reviewed. Based on a June 10, 1998, telephone conversation with Norma Rosner, Associate General Counsel, Vastar, neither ARCO nor Vastar have any interest in Indian leases producing coalbed methane that is transported and processed through the Val Verde System during the audit period. Therefore, this decision does not address Indian oil and gas interests or the regulations governing those interests, particularly the valuation regulations that were amended and recodified during the audit period. *See* 61 F.R. 5467 (February 12, 1996).

[3] MMS Unit No. 891-000538-A leases for which ARCO is the lessee are Leases Nos. 029-003385-0, 029-003403-0, 082-080711-0, and 082-080712-0. Also, numerous non-ARCO leases are committed to this unit.

Based on MMS's April 22, 1996, Dear Operator/Payor letter, the State determined that ARCO incorrectly calculated gross proceeds for the coalbed methane sales resulting in royalty deficiencies of $782,373 (FBIL 26974003). Further, MMS deemed ARCO's deficient royalty accounting to be systemic for all leases for which coalbed methane gas is transported through the Val Verde System and processed in the Val Verde Plant.

In the RVD Decision, RVD determined that the removal of $CO_2$ from coalbed methane produced from the San Juan Basin does not qualify for an extraordinary processing cost allowance in accordance with 30 CFR 206.158(d)(2)(1) (1989). The coalbed methane is transported and treated in the Val Verde Plant. ARCO/Vastar is charged a fee of $0.0778 per Mcf for $CO_2$ removal. All $CO_2$ removed in the Val Verde Plant during the audit period was vented to the atmosphere.

The issues of marketable condition and extraordinary processing cost allowances are identical for some of the leases in both the Order and the RVD Decision.[4] For other ARCO/Vastar leases, these issues are substantially similar and cover the same period and field and area. Therefore, the appeals from the Order and from the RVD Decision are consolidated.

The issues other than marketable condition and extraordinary gas processing cost allowances that are listed below are exclusive to gas produced form leases subject to the Order. All references to the Appellant's Statement of Reasons (SOR), Supplemental Statement of Reasons (SSOR), and Field Report (FR) responses cited in this decision are directed to the issues raised by the Order, unless otherwise specifically noted.

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[4] ARCO/Vastar's Leases Nos. 029-003385-0, 029-003403-0, 052-060711-0, and 082-080712-0 appear in both the Order and the RVD Decision.

*Issues*

1. Was the cost of $CO_2$ removal:

a.) necessary to place the gas in marketable condition, or b.) allowable as an extraordinary processing cost allowance?

2. Are costs incurred to transport the coalbed methane deductible?

3. Does the April 22, 1996, Dear Operator/Payor Letter violate the Administrative Procedure Act?

4. Is late payment interest applicable to royalties deemed deficient for prior periods?

1. *Analysis - $CO_2$ Removal*

a. Marketable Condition

ARCO/Vastar argues that the only requirement under the marketable condition regulation is for the lessee to place production in the physical condition necessary to market it under contracts typical for the field or area. SSOR at 10. Thus, ARCO/Vastar believes that the lessee is not required to condition the gas, i.e., remove $CO_2$ for "downstream markets." ARCO/Vastar cites *Beartooth Oil and Gas Co. v. Lujan*, CV 92-99-BLG-RWA (D. Mont. 1993), slip op. at 6 (opinion withdrawn after remand and settlement), in support of its position. *Id.*

For the period January 1989 through March 1992, ARCO/Vastar states that gas produced from the audited leases was sold arm's-length to Meridian Oil Inc. (Meridian) under the Unit Operating Agreement.[5] ARCO/Vastar claims that the gas was sold at the wellhead in marketable condition at the prevailing market price in the area. SSOR at 10. Several examples of wellhead sales of untreated coalbed methane are presented in an affidavit from Mr.

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[5] Unit Operating Agreement, San Juan 30-6 Unit area, between El Paso Natural Gas Company (Unit Operator) and various parties owning working interests in the unit.

Peter Edlund. *See* SSOR, Exhibit 4 at 2. "Since March 1992, ARCO has marketed their [sic] production under various selling arrangements." Order at 5. ARCO/Vastar cites *Xeno Inc.*, 134 IBLA 172 (1995), in support of its position that the production is in marketable condition at the wellhead. SSOR at 15.

As a corollary to the marketable condition issue, ARCO/Vastar avers that requiring royalty payment based on an arm's-length contract value increased by costs to place production in a downstream marketable condition violates the gross proceeds rule. ARCO/Vastar insists that the State cannot establish a value of the enhanced gas after post-sale transportation and $CO_2$ removal without taking into account allowable transportation and/or processing deductions. SSOR at 15.

In the Order, MMS asserts that the price received for wellhead production from January 1989 through March 1992 was derived from a wellhead sale from ARCO/Vastar to Meridian Oil Trading Inc., Meridian's affiliate. Based on third party information, the State determined that the wellhead prices offered by Meridian were reduced by costs associated with transporting the gas, and the processing to remove the $CO_2$ from the gas stream. Order at 5.

The State calculated royalties for coalbed methane from the audited leases by applying the valuation regulations in 30 CFR Part 206 (1989) and the guidelines contained in MMS's December 7, 1995, Royalty Policy Board Letter[6] as follows:

> On January 8, 1996, the State requested ARCO to provide a breakdown of costs associated with transporting the coalbed methane gas to the processing plant, any costs of dehydration prior to the CDP

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[6] The Royalty Policy Board Letter formed the internal basis for the subsequent April 22, 1996, Dear Operator/Payor Letter, which provided public guidance for valuing coalbed methane.

> [Central Delivery Point] and after the CDP, any costs associated with compression incurred to enhance production, or any compression necessary to move the gas to the processing plant, and costs associated with the removal of the $CO_2$ from the gas stream. ARCO's response to the State's request, was based on information received from Meridian by letter dated May 9, 1996, [which] stated the cost off [sic] the $CO_2$ removal was $.0778 per MCF.

Order at 5.

The Federal and Indian oil and gas valuation regulation's marketable condition rule provides as follows:

> The lessee is required to place gas in marketable condition at no cost to the Federal Government or Indian lessor unless otherwise provided in the lease agreement. Where the value established pursuant to this section is determined by a lessee's gross proceeds, that value shall be increased to the extent that gross proceeds have been reduced because the purchaser, or any other person, is providing certain services the cost of which ordinarily is the responsibility of the lessee to place the gas in marketable condition.

30 CFR 206.152(i) (1989).

The regulations define marketable condition as "lease products which are sufficiently free from impurities and otherwise in a condition that they will be accepted by a purchaser under a sales contract typical for the field or area." 30 CFR 206.151 (1989). Whether the gas was sold under a contract that is typical for the field or area from which it is produced is pertinent to the valuation issue here. Although ARCO/Vastar identifies several nominal sales of untreated coalbed methane for use in the area without

removal of the $CO_2$ (SSOR at 3-4), the dominant market for gas from the area is for gas with a lower $CO_2$ content.[7]

As ARCO/Vastar states, "[d]espite the active market for coalbed gas at the well, the total wellhead demand is limited by the lack of residential and industrial users in the region in which the field is located. Consequently, much of the gas must be transported to distant users . . . ." SSOR at 4. Furthermore, although ARCO/Vastar asserts that there could be an active end-user market for gas with a $CO_2$ content greater than 10 percent, such a market currently does not exist.[8]

Purchasers of gas from the field or area generally demand that the gas be properly conditioned for sale in the actual markets, which requires a lower $CO_2$ content. The fact that some purchasers are willing to purchase gas prior to conditioning and perform the conditioning themselves does not alter the finding that the gas needs to be conditioned. This is particularly true where the typical contracts for sales of gas from the field or area are in line with general national standards. The Department of the Interior cannot allow producers simply to alter the form of their sales arrangements in order to force the lessor to share in the producers' costs to place the product in marketable condition.

In *California Co. v. Udall*, 296 F.2d 384, 386 (D.C. Cir. 1961), the wellhead sales contract between The California Company and Southern Natural Gas Company required that the gas meet the quality and pressure specifications of

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[7] Based on the relatively current sales and utilization of gas in the field and area, gas with high $CO_2$ content (untreated) consists of less than 10 percent of Val Verde Plant capacity. (Derived from figures found at page 2 of the Edlund Affidavit.)

[8] ARCO/Vastar's arguments as to why pipeline transporters using tariffs based on energy content prefer not to transport gas with a high $CO_2$ content would apply equally to local distribution companies in distant markets.

the receiving pipeline. Consequently, the Department of the Interior disallowed the expenditures required to condition the gas to meet the pipeline specifications as production costs required to place the gas in marketable condition. *Id.* The court determined that the Secretary did not abuse his discretion by defining the statutory term "production" (for royalty purposes) as gas that is readied for the market into which it is sold. *Id.* at 388.

Here, there was little or no actual demand for the production in the condition extracted at the wellhead. Consequently, the value for royalty purposes must be determined by adding to the gross proceeds received from the wellhead purchaser the cost of treating the gas by the removal of $CO_2$ to the level required to place the gas in marketable condition. Thus, the portion of the appeal claiming that the gas is in a marketable condition at the time of sale at the wellhead is denied.

ARCO/Vastar lso argues that MMS's requirement to condition the gas to an interstate pipeline standard of two percent (2%) $CO_2$ content is arbitrary and contrary to law. SSOR at 11-13. I find that the mainline transporters' $CO_2$ quality requirements effectively establish a marketable condition standard for gas sold from the field or area.

In *California Co. v. Udall,* the quality standard that established the marketable condition of the production was the standard required by the receiving pipeline because the wellhead gas sales contract specifically required the pipeline standard for production quality.

Here, the gas must first meet the pipeline standard of quality before shipment to the market due to the absence of a viable market in the field or area. Therefore, the transportation of the production to a market outside the field or area is an integral part of marketing the gas.

There is only a very limited market for the gas in its wellhead condition. For a market to truly exist, there must

be "an established demand for an identified product." *California Co. v. Udall*, 296 F.2d at 388. There is no evidence that a market exists for the gas at issue unless it is conditioned to meet the mainline specifications. Thus, the minimum required condition of the coalbed methane for marketing (and royalty) purposes is the quality required to supply the market(s) where the demand exists.

The fact that ARCO/Vastar included a copy of the Southern California Gas Company tariff for transporting customer-owned gas to end users evidencing a marginally higher permitted $CO_2$ content (3%) than the current mainline requirements is of little import. MMS's regulations define marketable condition in terms of typical sales contract quality requirements for the field and area.[9] 30 CFR 206.151. The mainline quality requirements are reflective of the required condition of the gas for sales of production from the field or area. If the production does not meet mainline specifications for transport to the downstream interconnect or end use, the production is effectively unusable.

Based on the analysis above, this portion of the appeal is denied. However, the mainline quality standard (2% $CO_2$) used by the State in computing royalties does not agree with the mainline quality standards identified in the record for portions of the audit period (1-3% $CO_2$).[10] Therefore, the

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[9] As stated above, less than 10 percent of the coalbed methane is sold and utilized with a $CO_2$ content exceeding the mainline quality requirement at the wellhead. More than 90 percent of the production is treated to comply with the mainline quality specifications before being sold into market(s) outside the field and area. Thus, the "typical" sale of field and area coalbed methane occurs at the mainline $CO_2$ quality.

[10] The evidence in the record indicates that the mainline transporters' (El Paso Natural Gas, Transwestern, and Northwest Pipeline) $CO_2$ quality requirements vary from one to three percent (1-3%) content of coalbed methane volume over the audit period.

Order is modified and the Appellant must recalculate the royalties due for the audited leases during the audit period based on the content acceptable to the pipeline purchasers. The lessor will not share in treatment costs simply because one purchaser may require a marginally lower $CO_2$ content than another. Nor will the lessor require the lessee to condition the gas to a higher level of purity than the pipeline purchaser requires.

To summarize, the costs of $CO_2$ removal are the responsibility of the lessee when gas must be conditioned to meet the quality requirements typical for sales of gas from the field or area. Where there is no market for the gas at issue in the field or area, the marketable condition requirement is the quality of the mainline transportation to the downstream market. Thus, this portion of the appeal is denied and the Order is modified as explained above. The actual mainline quality specifications shall be used in all instances, including any quality specifications that were "grandfathered."

The above determination affects the coalbed methane subject to the RVD Decision as well as the Order. Where the costs of gas treatment are necessary to place production in marketable condition, those same costs cannot also be considered allowable as a cost to either transport or process the gas since gas conditioning must be performed cost-free to the lessor. 30 CFR 205.152(1) and 206.158(d)(1) (1989).

b. Extraordinary Processing Cost

As an alternative theory to including the cost of $CO_2$ removal as a cost of transportation (*see infra* section 2), ARCO/Vastar argues that it is entitled to an extraordinary processing cost allowance for removing $CO_2$ from the

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SSOR at Exhibit No. 5. Further, El Paso Natural Gas "grandfathered" the $CO_2$ allowed for mainline transportation from the Val Verde Plant at 2.13 percent. *Id.* (*See* Tariff No. 221 dated July 7, 1994).

coalbed gas stream regardless of whether the $CO_2$ was marketed and sold. Response to RVD Decision FR at 2. ARCO/Vastar points to MMS's approval of Louisiana Land and Exploration Company's (LL&E) extraordinary processing cost request to remove impurities (including $CO_2$) from its Lost Cabin Plant in Wyoming. Similar to $CO_2$ removed at the Val Verde Plant, the $CO_2$ removed at the Lost Cabin Plant was not marketed or sold.[11] Therefore, ARCO/Vastar argues that MMS's failure to grant it similar consideration regarding an extraordinary processing cost allowance for removing $CO_2$ that was not marketed and sold would result in an arbitrary and capricious application of the regulations. *Id.* at 2-3.

ARCO/Vastar also argues that MMS's March 19, 1996, Guidance for Extraordinary Processing Cost Allowance Applications (Guidelines)[12] clearly contemplate granting an extraordinary processing cost allowance when gas plant products are not sold.[13] *Id.* at 3. Lastly, ARCO/Vastar argues that methane is a product against which the extraordinary processing cost allowances may be deducted. *Id.* at 3-4.

The MMS argues that an allowance for processing may not be claimed for removal of the $CO_2$ because the $CO_2$ is not marketed and sold. (Instead, it is simply vented into the atmosphere.) Order at 3; RVD Decision at 5. The MMS

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[11] *See* Response to RVD Decision FR. Exhibit 4 at 1.

[12] Apparently, these same guidelines were issued by RVD (formerly Valuation and Standards Division at the time of issuance) on February 6, 1996. Whether this was an internal issue date versus the March issue date to the public is not clear from the record. Regardless, both documents will be treated as identical herein and will be referenced as the "Guidelines."

[13] *See* Response to RVD Decision FR, Exhibit 3 at 4.

will not grant an allowance for the cost of processing when the lease production is not royalty bearing.[14] *Id.*

The gas processing regulations provide:

> *Except as provided in paragraph (d)(2) of this section, no processing cost deduction shall be allowed for the costs of placing lease products in marketable condition*, including dehydration, separation, compression, or storage, even if those functions are performed off the lease or at a processing plant. Where gas is processed for the removal of acid gases, commonly referred to as "sweetening," no processing cost deduction shall be allowed for such costs unless the acid gases removed are further processed into a gas plant product. In such event, the lessee shall be eligible for a processing allowance as determined in accordance with this subpart. *However, MMS will not grant any processing allowance for processing lease production which is not royalty bearing.*

30 CFR 206.158(d)(1) (1989) (emphasis added).

Although the concept of marketable condition described above includes the processes of dehydration, separation, compression, and storage, the list is illustrative and is not all-inclusive. Placing production into marketable condition includes any process used to treat or condition gas (remove impurities) necessary to meet contract quality specifications. 30 CFR 206.151. Thus, the processing of gas for the purpose of removing impurities falls within the concept of placing production in marketable condition.

As determined in section 1.a, above, the removal of $CO_2$ is required to place the production in marketable condition. The $CO_2$ is not captured and sold and is not a royalty-

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[14] The RVD Decision implies that an extraordinary cost processing allowance will not be granted in the absence of a processing allowance for that same gas plant product. *See* Decision at 5.

bearing product. Under the facts of this case, $CO_2$ is an impurity. In accordance with the gas processing regulations, "no processing cost deduction shall be allowed for the costs of placing lease products in marketable condition." 30 CFR 206.158(d)(1). However, processing circumstances qualifying under subsection 30 CFR 206.158 (d)(2) may result in an exception to the marketable condition requirement of subsection (d)(1). Thus, the question arises whether the requirement that the lease production be royalty-bearing precludes granting of an extraordinary processing cost allowance for removing $CO_2$ as well as a processing allowance.

For purposes of this decision, however, it is not necessary to resolve that issue because ARCO/Vastar fails to meet the requirements of paragraph (d)(2) in any event. Section 206.158(d)(2)(i) provides:

> If the lessee incurs extraordinary costs for processing gas production from a gas production operation, it may apply to MMS for an allowance for those costs which shall be in addition to any other processing allowance to which the lessee is entitled pu[r]suant to this section. Such an allowance may be granted only if the lessee can demonstrate that the costs are, by reference to standard industry conditions and practice, extraordinary, unusual, or unconventional.

ARCO/Vastar argues that the amine process[15] used in the Val Verde Plant to extract the $CO_2$ *meets the criteria of paragraph (d)(2) to qualify as an extraordinary processing allowance for the costs of $CO_2$ removal* [emphasis added] because: 1) the gas stream is atypical, 2) the process used to remove $CO_2$ is unique, and 3) the costs of $CO_2$ removal are extraordinary. Response to RVD Decision FR at 2-7; SOR to RVD Decision at 2-4. ARCO/Vastar believes that

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[15] The amine process in the Val Verde Plant utilizes diethanolamine or DEA.

coalbed methane treatment at the Val Verde Plant is similar to processing of production entering Exxon Corporation's LaBarge facility, and that IBLA's Decision in *Exxon Corp.*, 118 IBLA 221 (1991), should control. SSOR at 16-18.

The RVD determined that ARCO/Vastar's costs of extracting $CO_2$ from the coalbed methane at the Val Verde Plant do not qualify as an extraordinary processing allowance. The RVD argues that: 1) the uniqueness of the gas stream is debatable, 2) the amine process is not unconventional, and 3) the costs of extracting $CO_2$ do not appear to be extraordinary. RVD Decision at 6.

The MMS's March 1996 Guidelines were issued to provide further explanation of the criteria relevant to determining whether particular gas meets paragraph (d)(2)'s requirements. The criteria focus on gas composition, plant processes, and cost of plant processes relative to what is considered those same factors for "standard" gas processing plants. Guidelines at 2. (The criterion of "atypical" gas arose in the MMS's *Oil and Gas Payor Handbook, Volume III* (*Payor Handbook*), released July 21, 1993, but no additional guidance on the other criteria was provided in that release.) In addition, MMS issued a "Dear Operator/Payor Letter" on April 22, 1996, that specifically addressed coalbed methane valuation and reporting, but these guidelines do not address the applicability of extraordinary processing cost allowances.[16]

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[16] The Guidelines in the April 1996 Dear Operator/Payor Letter did not fully convey MMS's Royalty Policy Board's (Board) findings regarding processing allowances applicable to $CO_2$. The Board addressed the issue of extraordinary processing cost allowances for coalbed methane by concluding that where $CO_2$ is vented and not sold, the cost of the $CO_2$ extraction process is not warranted. *See* MMS Royalty Policy Board Guidelines (December 7, 1995) at 2-3.

ARCO/Vastar argues that the coalbed methane stream is "atypical" due to its composition, and unlike a conventional gas stream, the coalbed gas' composition changes over time. SSOR at 17. ARCO/Vastar's coalbed gas compositional analyses from three Central Delivery Points (CDP's) serving the audited leases reveals between 83.87 to 87.08 percent methane, 12.65 to 15.86 percent $CO_2$, 0.23 to 0.35 percent ethane, and trace amounts of nitrogen. Response to RVD Decision FR at Exhibit 5.

The RVD argues that "no liquid hydrocarbons does not make [ARCO/Vastar's coalbed gas] unusual," that the $CO_2$ content "is not a compelling argument for classifying the gas as unusual or atypical," and that the large volume of this particular composition "makes it difficult to classify this gas as unusual or atypical." RVD Decision at 4. The RVD concludes that "[t]he pertinent factor ... is whether the chemical composition of the gas stream required processing of an extraordinary, unusual or unconventional nature." *Id.* In the RVD Decision Field Report, RVD argues that the definition of atypical in the *Payor Handbook* is not formal and that the "*regulations provide that cost, not composition, is the determining factor in granting an extraordinary processing cost allowance.*" RVD Decision FR at 6 (emphasis in original).

The sole source where MMS defines "atypical" is in its *Payor Handbook.*[17] This definition was derived from the first Departmental approval of an extraordinary processing cost allowance.[18] The term appears to describe the nature of the gas stream in the *LL&E* and *Exxon* decisions by

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[17] "Atypical" gas is defined as gas that does not contain liquefiable hydrocarbons, such as ethane, propane, butane, etc." *Payor Handbook* at 7.1.2.

[18] *See* August 13, 1992, Assistant Secretary for Land and Minerals Decision in *Exxon Corporation* (citing the atypical nature of the gas stream with no liquefiable hydrocarbons).

alluding to the absence of liquefiable hydrocarbons in the respective gas streams. However, the more important aspect of designating a gas stream as atypical is where the *Payor Handbook* requires the determination in order to further consider the other aspects of approving an extraordinary processing cost allowance.[19] *See Payor Handbook* at 7.1.2. Thus, the degree to which a particular gas stream is atypical is not as important as the atypical designation itself as a threshold determination in approving an extraordinary processing cost allowance.

Because the *Payor Handbook* is the sole source of defining atypical and because of the threshold emphasis the *Payor Handbook* places on the atypical designation, ARCO/Vastar's gas stream at issue here qualifies as atypical. However, this determination is not dispositive of the extraordinary processing cost allowance issue, but simply begins the analysis.

ARCO/Vastar argues that the Val Verde Plant process is unconventional and complex because the amine process used to remove $CO_2$ is chemical versus the physical extraction processes used to typically extract natural gas liquids. Also, ARCO/Vastar argues that the amine process is distinguishable from other plants that use amine because the Val Verde Plant uses a greater percentage of amine, which requires much more water, and the plant requires stainless steel in certain areas versus carbon steel used in other amine plants. SSOR at 17. The technical features of the Val Verde Plant alluded to above are described in two engineering papers[20] contained in the record. Response to

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[19] The Guidelines are silent concerning the atypical nature of the gas stream. Instead, the Guidelines focus on whether the gas stream composition either is unusual compared to conventional gas streams or is similar to previously determined unconventional gas streams.

[20] *See, e.g.*, Anderson, *Comparison of Val Verde Plant to LaBarge Plant.* SOR at Exhibit 10: Anderson, *The Treatment of Coal Seams*

RVD Decision FR at 6. Lastly, ARCO/Vastar argues that a gas processing plant does not have to be "one-of-a-kind" in order to be eligible for an extraordinary processing cost allowance. *Id.*

The RVD argues that the amine process used in the Val Verde Plant for $CO_2$ removal is neither unconventional nor extraordinary. The RVD also argues that the Val Verde Plant design and equipment utilizing the amine process is "much the same for both coalbed and non-coalbed gas plants." RVD Decision at 5: RVD Decision FR at 8-9.

ARCO/Vastar argues that the amine process is complex and unusual by focusing on the type, concentration, and amount of amine (requiring use of 316L stainless steel), and the amount of water required. The use of amine processes in gas processing plants is quite common. ARCO/Vastar's arguments that its amine process is unusual primarily address the plant's larger size and throughput volumes. Compared to a conventional gas processing plant, the Val Verde Plant lacks any of the equipment necessary to extract natural gas liquids or to recover sulfur. Thus, the Val Verde Plant is composed of only one part of what is considered a fairly complex natural gas processing plant.[21] Given the lack of plant complexity and the common nature of the amine process, the Val Verde Plant is neither unconventional nor extraordinary.

ARCO/Vastar argues that the $0.0778 per Mcf cost to recover methane is significant. SSOR at 17: Response to RVD Decision FR at 7.

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*Gas at Val Verde Plant* (1992). Response to RVD Decision FR at Exhibit 6.

[21] The MMS considers Exxon's LeBarge Plant and LL&E's Lost Cabin Plant to represent complex gas processing plants. The cost to process methane in these plants is substantially greater than the costs claimed by ARCO/Vastar to be significant.

The RVD claims that ARCO/Vastar's cost is at the low end of the range of $CO_2$ removal. RVD Decision FR at 10.

The issue in determining the qualification of processing costs as an extraordinary allowance is the extent of the costs incurred by reference to standard industry costs. 30 CFR 206.158(d)(2)(1). Here, ARCO/Vastar simply refers to the costs as significant, but the record contains no documentation demonstrating that the costs represent an extraordinary rather than a typical expense for the treatment performed. Therefore, in the absence of substantiating the extraordinary nature of processing costs with reference to standard industry costs, ARCO/Vastar's application for an extraordinary processing cost allowance must be denied in any event.

The conclusion above regarding the non-qualification of $CO_2$ removal costs as an extraordinary gas processing cost allowance applies to both the Order and the RVD Decision. The Order and RVD Decision are modified to the extent necessary to conform to the decision above.

2. *Analysis - Transportation*

The MMS states in the Order that "[t]ransportation allowances are granted for the reasonable, actual necessary costs of transporting the coalbed methane from the royalty measurement point (either the well or the Central Delivery Point (CDP) [)] to the point of sale remote from the lease." Order at 2. Further, "no allowance may be taken for the costs of transporting lease production which is not royalty bearing without MMS approval." 30 CFR 206.157(a)(2)(i) (1989).

The transporters at or near the tailgate of the Val Verde Plant (e.g., El Paso Natural Gas Company, Transwestern Pipeline Company, and Northwestern Pipeline Company) currently specify in their transportation agreements that the gas quality cannot exceed two percent of $CO_2$ for

mainline transport."[22] In addition, the guidance provided by MMS states that "transportation costs [can only be] allocated to the methane component for the amount of $CO_2$ permitted in the main (inter- or intrastate) transmission line." April 22, 1996, Dear Operator/Payor Letter at 2. Consequently, the State disallowed costs to transport $CO_2$ exceeding two percent of the combined volume of gas.

The Appellant argues that the State is restricting the allocation of transportation costs to gas that is at the interstate pipeline standard of two percent $CO_2$ and that the State considers $CO_2$ in excess of that standard a non-royalty bearing product. However, the Appellant contends that the cost of transporting $CO_2$ should be included as part of the transportation allowance for methane because unmarketable $CO_2$ is a waste product to which no allocation of transportation costs should apply in accordance with 30 CFR 206.157(a)(2)(1) (1989). SSOR at 14.

Further, ARCO/Vastar states that the primary reason for removing the $CO_2$ is to transport the gas stream, not to place it in marketable condition. ARCO/Vastar concludes that $CO_2$ removal should be treated the same as the dehydration costs in *Exxon*, 118 IBLA at 221, and the liquefaction costs in *Marathon Oil Co. v. United States*, 604 F. Supp. 1375 (D. Alaska 1985), *aff'd* 807 F.2d 759 (9th Cir. 1986), *cert. denied*, 480 U.S. 940 (1987). SSOR at 16. I disagree with the Appellant's contentions.

a. *January 1989 - March 1992*

For the period January 1989 through March 1992, all of ARCO/Vastar's gas was sold at the wellhead, but it was not in marketable condition, as determined in section 1 above. The "Gas Gathering and Treating Agreement" between MOGI and ARCO Oil and Gas Company dated December 17, 1990, applicable to the audited leases specifies a fee of

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[22] *See supra* note 10.

$0.36 per Mcf for treatment and transportation. Because the treatment fee is $0.0778 per Mcf, the remainder of the fee is for transportation.

The State argues that since approximately $0.2822 per Mcf is charged for transporting the entire coalbed methane stream, the portion of the fee applicable to the $CO_2$ content in excess of the mainline allowable cannot reduce the value of the production used to calculate the royalty. The payment received for sales under the Unit Operating Agreement at the wellhead reflected a reduction of the sales price for the cost of treating and transporting the coalbed methane and the $CO_2$.[23] Since the Appellant's sales price at the wellhead or CDP during the period January 1989 through March 1992 included a reduction for not only the transportation of the methane and the 2% $CO_2$ allowed of mainline transport but also a reduction for transportation of the remainder of the $CO_2$ to the Val Verde Plant, the value used to calculate the royalty must include not only the sales price of the coalbed gas stream, but also the amount of non-allowable reduction of the sale price for transportation of the $CO_2$ in excess of the 2%.

The costs of transporting the $CO_2$ component above the mainline standards, which are costs of transporting a non-royalty-bearing product as addressed in section 2.c. below, must be added to the lessee's wellhead gross proceeds. This is in keeping with the principle that the Department cannot allow producers to simply alter the form of their sales arrangements in order to force the lessor to share in

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[23] The Appellant stipulates that its wellhead sales were to Meridian Oil Inc. SSOR at 10. MOGI provides the services under the "Gas Gathering and Treatment Agreement" to the Appellant. Because of the inter-relationships between the coalbed methane sales and its treatment, the State claims that "third party" information verifies that the Meridian affiliates incorporated (deducted) the cost of treatment and transportation into the production's market value at the Val Verde Plant.

costs in which it does not otherwise share. Also, the transportation of the $CO_2$ to the treatment plant in this instance is a service that is inextricably tied to placing the gas in marketable condition because the $CO_2$ is extracted at the plant. Thus, the lessee's gross proceeds must be increased to the extent they have been reduced because the purchaser was providing these services to place the production in marketable condition. *See* 30 CFR 206.152(i). Thus, this portion of the appeal is denied.

b. *Post March 1992*

For all gas that is sold downstream of the wellhead or CDP, a transportation allowance may be applicable. "Since March 1992, ARCO has marketed their production under various selling arrangements." Order at 5. However, evidence of the "various selling arrangements" is not contained in the record. For these sales of gas, the regulations at 30 CFR 206.156 and 206.157 (1989) govern applicable transportation allowances subject to the determination in part 2.c. below.

c. *Transportation of Waste*

ARCO/Vastar argues that the State incorrectly computes the allowable costs of $CO_2$ transportation both from the wellhead/CDP to the plant and from the plant to the point of sale. ARCO/Vastar contends that allocation to the methane stream of the costs of transporting a $CO_2$ waste product comports with the valuation regulations and that there is no reason for treating amounts of "waste" $CO_2$ within interstate pipeline standards, i.e., less than two percent, differently than amounts in excess of those standards. SSOR at 13-15. I disagree.

The issue of transporting $CO_2$ in excess of the mainline quality standard downstream of the Val Verde Plant has already been addressed, in effect, by the marketable condition determination in section 1 above. In other words, because the coalbed methane must be placed in a marketable

condition prior to mainline transportation, there are no $CO_2$ volumes that must otherwise be transported downstream of the plant. Thus, the sole issue regarding $CO_2$ waste volumes pertains to the transportation of the coalbed methane from the wellhead to the Val Verde Plant for the remainder of the audit period commencing May 1992.

The guidance provided by the *Payor Handbook* notes that "[t]ransportation costs for a gaseous stream [or a liquid and gaseous stream] are allocated only to the royalty-bearing and non-royalty-bearing products. For transportation cost allocation purposes, a waste product is considered neither royalty-bearing nor non-royalty-bearing. Therefore, the waste product volume is excluded from the cost allocation." *Payor Handbook* 6.4.1.

The three examples contained in section 6.4 of the *Payor Handbook* all assume that $CO_2$ is a waste product. Additional guidance is contained in the April 22, 1996, Dear Operator/Payor Letter. In assessing additional royalties on ARCO/Vastar for transportation of $CO_2$ volumes, MMS followed the guidance in the Dear Operator/Payor Letter, which states:

> For coalbed methane production, you can increase the transportation costs allocated to the methane component for the amount of $CO_2$ permitted in the main (inter- or intrastate) transmission line. For example, if your gas stream consists of 90 percent methane and 10 percent $CO_2$ and the main transmission line allows 2 percent $CO_2$ in the makeup of its gas stream, you can include the costs of transporting the 2 percent $CO_2$ volume (or 92 percent of the total transportation cost) when calculating your allowance for methane.

Dear Operator/Payor Letter at 2.[24]

The valuation regulations address waste as follows:

> [T]he total transportation costs shall be allocated in a consistent and equitable manner to each of the products transported in the same proportion as the ratio of the volume of each product (excluding waste products which have no value) to the volume of all products in the gaseous phase (excluding waste products which have no value). Except as provided in this paragraph, no allowance may be taken for costs of transporting lease production which is not royalty bearing.

30 CFR 206.157(a)(2)(i); 206.157(b)(3)(i).

The preamble to the revised valuation regulations published in the *Federal Register* on January 15, 1988, provides:

> The MMS does not agree with the commenters' proposal that the cost of transporting nonroyalty-bearing substances should be shared by the lessor in all instances. However, upon review, MMS has recognized that it is appropriate to provide an allowance which includes the costs of transporting certain nonroyalty-bearing substances such as waste products, including water. For example, there may be circumstances where transportation of water along with the royalty-bearing portion of the production is necessary. For other than waste products, the final rule provides, however, that prior MMS approval is required before an allowance may be taken for the costs of transporting non-royalty-bearing substances.

53 F.R. 1230, 1258 (1988).

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[24] A Dear Payor Letter issued February 4, 1988, also addresses transportation cost allocation among produced products, but it does not contain the $CO_2$ instructions issued in the April 22, 1996, Dear Operator/Payor Letter. *See supra* note 6.

The regulations do not specifically explain the distinction between "non-royalty-bearing products" and "waste products." The guidance provided in the Dear Operator/Payor Letter treats $CO_2$ as a non-royalty-bearing product, but then directs the operator/payor to "use the regulation in 30 CFR 206.156 and 206.157 (1995) and the instructions in Chapter 6 of the *Oil and Gas Payor Handbook, Volume III*, to calculate your transportation allowance."

Arguably, one could infer from the *Payor Handbook* hypotheticals that $CO_2$ in this situation is assumed to be a "waste product." To do so, however, would be incorrect.[25]

The intent of the *Payor Handbook* examples is apparent. Proportionate measures of the identified gas stream constituents affect the computation of transportation allowances. Had the numbers given in the examples represented volumes instead of Btu's, the results would have been what MMS intended. The reference to $CO_2$ as a waste product would also have made sense with respect to the regulations.

The MMS allocates the cost of transporting the mainline allowable non-methane constituents in a gas stream to the methane component. This is the only portion of the non-royalty-bearing production that is considered a waste product. Even in the *Payor Handbook* examples, the fraction of $CO_2$ in the examples represented typical mainline allowables; representing from one to two-and-one-half percent (1-2½%) of the heating value (sic) of the gas stream.

The Dear/Operator/Payor Letter guidance primarily treats the $CO_2$ content that was removed from the coalbed

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[25] The *Payor Handbook* examples at 6.4.1, 6.4.2, and 6.4.3 contain unfortunate ambiguities. They refer to gas streams that have MMBtu measures of $CO_2$ and helium. Neither $CO_2$ nor helium have energy contents (Btu's). Thus, the hypothetical examples are difficult to apply because we have no idea of the volumes of these gas stream constituents upon which to compute transportation allowances.

methane as a non-royalty-bearing product. Only the pipeline allowable $CO_2$ content (remaining in the methane stream) is treated as a waste product.[26] The fact that a small amount of waste product remains is primarily the result of inefficiencies involved in further removal. Beyond a point, inefficiencies of removal processes and/or pipeline tolerances[27] dictate against further removal of impurities, which then become a waste product (as opposed to its non-royalty bearing status if present in amounts greater than the quality specifications of the mainline).

The valuation regulations specify that transportation costs are to be allocated to all royalty-bearing products after excluding waste products, both from the total volume and from the volume of all products. 30 CFR 206.157(a)(2)(i); 206.157(b)(3)(i). In addition, the preamble providing the rationale for these regulations clearly indicates that the cost to transport non-royalty-bearing products that are not waste products will not be included in the allowable transportation deduction for royalty-bearing products. 53 F.R. 1230, 1258 (1988). The preamble implication that MMS will approve an allowance for the costs to transport non-royalty-bearing substances is limited to those non-royalty-bearing substances that are also waste products as defined above. *Id.*

Here, the $CO_2$ produced in conjunction with the methane from the coalbed is transported to a treatment plant, separated (save for two percent content) from the methane, and vented. There is no market for this $CO_2$. The intent of MMS's regulations and *Payor Handbook* is that waste

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[26] The cost to transport the interstate pipeline allowable $CO_2$ content is allocated to the methane and allowed as a cost of transporting the methane. *See* Dear Operator/Payor Letter at 2.

[27] Pipeline tolerances used in this context refers to the physical ability of the pipeline to operate efficiently at certain levels of non-methane constituents or contaminants.

production for the purpose of determining allowable transportation costs is the fraction of non-royalty-bearing product that is allowable in a mainline transportation system. In the instant case, all $CO_2$ in excess of the mainline standard is non-royalty-bearing production. Therefore, this portion of the appeal is denied.

Consistent with the modification in section 1 above, the mainline standard of allowable $CO_2$ (2% $CO_2$) used by the State in computing royalties does not agree with the mainline quality standards identified in the record for portions of the adult period (1-3% $CO_2$).[28] Therefore, the Order is modified and the Appellant must recalculate the royalties due for the audited leases during the audit period based on the guidance above.

3. *Analysis - Administrative Procedure Act*

ARCO/Vastar avers that the State is applying the April 22, 1996, Dear Operator/Payor Letter as a rule in violation of the Administrative Procedure Act (APA). 5 U.S.C. 551-559, 701-706 (1994). In support of its position, the Appellant cites *Phillips Petroleum Co. v. Johnson*, 22 F.3d 616 (5th Cir. 1994), *cert. denied*, 514 U.S. 1092 (1995). Under *Phillips*, the court determined that the APA required notice and comment rulemaking for the valuation procedures at issue in that case. In addition, ARCO/Vastar argue that the supposedly newly-instituted procedures cannot be applied retroactively. SSOR at 18-21.

Here, the State applied the existing valuation regulations which were further explained by the April 22, 1996, Dear Operator/Payor Letter. To the extent that the State's interpretation was inconsistent with the regulations, this decision modifies the Order to make it consistent with the regulations.

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[28] *See supra* note 10.

When, through notices or interpretive rules, the Government explains and clarifies existing regulations, the procedural requirements of rulemaking under the Administrative Procedure Act, 5 U.S.C. 553 (1982), are not applicable. *Venlease I*, 99 IBLA 387 (1987). *See Shalala v. Guernsey Memorial Hospital*, 514 U.S. 87, 115 S. Ct. 1232 (1995). The Dear Operator/Payor Letter is an interpretation of existing regulations. Therefore, this portion of the appeal is denied.

4. *Analysis - Late Payment Interest*

The Appellant argues that it would be inequitable to assess late payment interest on royalties due based on a valuation procedure that could not have been anticipated by lessees. SSOR at 21.

Assessments of late payment charges are supported by longstanding precedent. *See Gary-Williams Energy Corporation*, MMS-91-0366-IND (May 15, 1992). 13 Gower Federal Service, Royalty Valuation and Management, Rocky Mountain Mineral Law Foundation, and cases therein cited. In *Gary-Williams*, the Appellant's challenge to the late payment assessment was limited to the application of a new valuation procedure. Inasmuch as the valuation procedure was determined to be interpretative of existing regulations, the assessment was proper. *See Columbia Gas Development Corp.*, 123 IBLA 395 (August 7, 1992) (holding that the late payment assessments were appropriate since the underpaid lease remained in an underpaid status for several months until a corrected Form MMS-2014 was filed).

The same reasoning applies in this appeal since the valuation procedure was, like in *Gary-Williams*, an interpretation of existing regulations. Accordingly, the late payment assessment must be sustained.

*Conclusion*

1. Was the cost of $CO_2$ removal a.) necessary to place the gas in marketable condition, or b.) allowable as an extraordinary processing cost allowance? The gas was not in marketable condition for its object market. The cost to place the production into marketable condition is to be borne by the lessee at no cost to the lessor. Thus, the arm's-length proceeds received for the wellhead sale of gas must be adjusted for the cost of placing the gas in marketable condition. The removal of $CO_2$ from the coalbed gas stream is required to place the gas in marketable condition. Costs to place gas in marketable condition do not qualify as costs of processing.

Further, the cost to remove $CO_2$ from the gas stream does not qualify as an extraordinary gas processing allowance because the Val Verde Plant process and costs incurred to remove $CO_2$ do not qualify as extraordinary, unusual, or unconventional by reference to standard industry costs for similar $CO_2$ removal processes.

2. Are costs incurred to transport coalbed methane deductible?

When gas is sold at the wellhead, transportation costs are not allowed to be deducted from the value of production for royalty purposes. Costs to transport non-royalty-bearing production to enable the production to be placed in a marketable condition are not allowed, except to the extent that the mainline transporter allows a specified amount.

When the lessee transports gas from the lease to a point of sale away from the lease, the cost to transport the gas may be allowable. The cost to transport gas is not allocable to waste products, but is allocable to royalty-bearing and non-royalty-bearing, non-waste production. The portion of the cost allocated to non-royalty-bearing product is not deductible as an allowance. Waste is defined as the mainline

allowable portion of a particular non-methane constituent of the gas.

3. Does the April 22, 1996, Dear Operator/Payor Letter violate the Administrative Procedure Act?

The Dear Operator/Payor Letter is an interpretive guide to existing regulations. Thus, the procedure contained in the Dear Operator/Payor Letter does not violate the Administrative Procedure Act.

4. Is late payment interest applicable to royalties deemed deficient for prior periods?

The lessee cannot avoid late payment interest assessed on unpaid royalty for prior periods.

ARCO/Vastar must recalculate the royalties due accordingly.

Because this decision is issued by an Assistant Secretary of the Department of the Interior, it is not subject to appeal to the Interior Board of Land Appeals and is the final action of the Department. *Blue Star Inc.*, 41 IBLA 333 (1979); *Marathon Oil Co.*, 108 IBLA 177 (1989).

Sincerely

/s/ Sylvia V. Baca
Sylvia V. Baca
Assistant Secretary, Land
and Minerals Management

## APPENDIX G

[Seal Omitted]

# United States Department of the Interior

MINERALS MANAGEMENT SERVICE

Royalty Management Program
P.O. Box 25165
Denver, Colorado 80225-0165

MMS/RVD-OG: 97-0315
Mail Stop 3152 February 26, 1998

Memorandum

To: Chief, Appeals Division
Policy and Management Improvement

From: Chief, Royalty Valuation Division
/s/ Deborah Gibb Tschudy

Subject: Field Report on Appeal by Vastar Resources, Inc. (Vastar) Regarding Denial of Extraordinary Processing Cost Allowance, Appeal Docket No. MMS-97-0191-O&G

By letter dated August 14, 1997 (Attachment 1), Vastar appealed Royalty Valuation Division's (RVD) decision of July 14, 1997 (Attachment 2), denying Vastar's application for an extraordinary processing cost allowance (Attachment 3). The appeal was timely filed and assigned Docket No. MMS-97-0191-O&G (Attachment 4). RVD granted Vastar extensions to file its Statement of Reasons (SOR) until October 16 and November 12, 1997 (Attachment 5). The extensions prolong for 87 days the 33-month time frame for processing appeals as set out in 30 U.S.C. 1725(h)(l) and any time frame Minerals Management Service (MMS) may provide for by regulation. Vastar submitted to SOR (Attachment 6) on November 12, 1997.

Vastar has requested the subject appeal be consolidated with appeal Docket No. MMS-97-0063-O&G (Attachment 7).

Because RVD is not a party to that appeal, we address only the issue of an extraordinary processing cost allowance to appeal here. However, to the extent the two appeals overlap with respect to extraordinary processing cost allowances, this report will also apply to appeal Docket No. MMS-97-0063-O&G.

## ISSUE

At issue is whether Vastar's coalbed gas (also called coalbed methane) is eligible for an extraordinary processing cost allowance.

## RECOMMENDATION

We recommend the appeal be denied on the grounds that Vastar's coalbed gas does not qualify for an extraordinary processing cost allowance.

## BACKGROUND

Vastar produces coalbed gas from leases in the San Juan Basin, New Mexico. The gas contains carbon dioxide ($CO_2$) in excess of that allowed by the major pipelines servicing the area.[1] The gas is gathered by Burlington Resources Inc. (Burlington) and treated at Burlington's Val Verde Gas Plant to remove the excess $CO_2$.

The Val Verde Plant employs the amine process to remove $CO_2$ from the gas stream. The extracted $CO_2$ is vented to the atmosphere. Burlington does not charge an individual

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[1] El Paso Natural Gas Company permits a maximum 2.13 percent $CO_2$ for gas entering its pipeline from the Val Verde Plant. Other major gas transportation companies servicing the San Juan Basin generally permit a maximum 2 percent $CO_2$ in their pipelines. Although Vastar does not give its coalbed gas composition, its leases are located in the "overpressured, high $CO_2$ area" of the San Juan Basin. Coalbed gas from this area typically consists of 85 to 100 percent methane, less than 1 percent to more than 13 percent $CO_2$, and negligible amounts of liquid hydrocarbons (natural gas liquids) and nitrogen. Gas entering the Val Verde Gas Plant averages about 11.3 percent $CO_2$.

fee for the $CO_2$-removal service.[2] Rather, the cost of removing the $CO_2$ is part of a bundled services fee that Burlington charges for both gathering the coalbed gas from the production field and treating the gas (removing the $CO_2$) at the Val Verde Plant. In response to MMS's policy on coalbed gas valuation, Burlington attributes $0.0778/Mcf of the bundled services fee to $CO_2$ removal.

Vastar seeks an extraordinary processing cost allowance pursuant to 30 CFR § 206.158(d)(2) (1997) to deduct from royalty value the costs charged by Burlington for extracting the $CO_2$. In its allowance application (Attachment 3), Vastar contended that the composition of the gas stream, plant design, and costs are sufficiently extraordinary to warrant such an allowance. RVD determined in its July 14, 1997, decision that the gas does not qualify for an e. ordinary processing cost allowance. Attachment 2 gives the rationale for our decision and is incorporated herein by reference as support of this field report. Vastar's arguments in its SORs remain much the same as in its allowance application.

Vastar continues to assert that an extraordinary processing cost allowance is proper because it meets the criteria set forth in MMS's processing cost allowance guidelines (Attachment 8) and the requirements in 30 CFR § 206.158(d)(2). Specifically, Vastar contends:

1. The composition of the gas stream is atypical when compared to conventional gas (SOR for MMS-97-0191-O&G at p. 2). (Vastar originally argued the gas was "unique.")

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[2] Vastar did not submit its gathering and treating agreement with Burlington. However, it is common knowledge that Burlington and other companies that gather and treat coalbed gas in the San Juan Basin charge bundled services fees.

2. The $CO_2$-removal process is more than conventionally used to process gas (SOR for MMS-97-0063-O&G at p. 17).
3. The unit cost to recover the principal product, methane, is significant (SOR for MMS-97-0063-O&G at p. 17).

Vastar also argues:

4. The composition of the gas stream and processing techniques is in several respects comparable to the circumstances in *Exxon Corp.*, 118 IBLA 221 (1991), in which the Interior Board of Land Appeals (IBLA) found that an extraordinary processing cost allowance was proper (SOR for MMS-97-0191-O&G at p. 2).
5. RVD's application denial is so consistent with MMS's prior interpretations of the regulations and guidelines as to be arbitrary and capricious (SOR for MMS-97-0191-O&G at p. 2).

Arguments 1 through 3 form the factual core of Vastar's appeal. Although RVD addressed these arguments in its denial decision (Attachment 2), we further elaborate on them here. Arguments 4 and 5 are ancillary to the main issue; we only comment on these arguments for informational purposes.

## APPLICABLE REGULATIONS AND GUIDELINES

### Regulations

Pertinent rules governing processing allowances are found in 30 CFR § 206.158 (1997) as follows:

- First, 30 CFR § 206.158(a) (1997) permits the lessee to claim a deduction (a "processing allowance") for its reasonable, actual costs of processing when gas is processed. Regulations at 30 CFR § 206.151 (1997) define "processing" as any process, including absorption, or refrigeration, designed to remove elements or

compounds (hydrocarbon or nonhydrocarbon) from the natural gas stream.

- Second, 30 CFR § 206.158(b) (1997) directs that processing costs must be allocated among the gas plant products. Regulations at 30 CFR § 206.151 define "gas plant products" as separate marketable elements, compounds, or mixtures resulting from processing gas, excluding residue gas (methane). (Carbon dioxide can qualify as a gas plant product.)
- Third, 30 CFR § 206.158(c)(1) (1997) provides that a processing allowance cannot be applied against the value of the residue gas, unless MMS grants an extraordinary processing cost allowance.
- Fourth, 30 CFR § 206.158(c)(2) (1997) limits the processing allowances to 66 2/3 percent of the transportation-adjusted value of each gas plant product. MMS may approve a greater allowance under the companion rule at 30 CFR § 206.158(c)(3) (1997), but the greater processing allowance cannot reduce the value of any gas plant product to zero. (In applying this rule, MMS will grant a processing allowance up to 99 percent of the value of a gas plant product.)
- Fifth, 30 CFR § 206.158(d)(1) (1997) provides that no processing cost deduction shall be allowed for the costs of placing lease products in marketable condition, unless otherwise approved through an extraordinary cost allowance. This regulation further states that no deductions shall be allowed for the costs of removing acid gases, commonly referred to as "sweetening," unless the acid gases removed are further processed into gas plant products (meaning marketable products under the definition at 30 CFR § 206.151). (Carbon dioxide is an acid gas.) This regulation also provides that MMS will not grant any pro-

cessing allowance for processing lease production that is not royalty bearing.

- Finally, 30 CFR § 206.158(d)(2)(i) (1997) permits a lessee to apply for an extraordinary processing cost allowance, if such costs are incurred. However, the lessee must demonstrate that the costs are extraordinary, unusual, or unconventional by reference to standard industry conditions and practice. This regulation states that the extraordinary processing cost allowance shall be in addition to any other processing allowance to which the lessee is entitled.

**Extraordinary Processing Cost Allowance Guidelines**

MMS issued guidelines for preparing and reviewing extraordinary processing cost allowance applications on March 19, 1996 (Attachment 8). Under these guidelines, MMS considers one or more of the following factors to determine whether an extraordinary processing cost allowance is appropriate:

- The composition of the gas stream being processed.
- The complexity of the gas plant design compared to conventional or typical gas processing plants, as well as methods (absorption, adsorption, refrigeration, cryogenic, etc.) used to process the gas to remove elements or compounds (hydrocarbon or nonhydrocarbon) from the gas.
- The unit costs incurred to recover the principal product, usually methane.

MMS evaluates these factors to determine if they are clearly extraordinary in relation to other gas plants.

**Coalbed Gas Guidelines**

MMS's Royalty Policy Board (Board) issued guidelines for valuing and reporting coalbed gas (coalbed methane) on December 7, 1995 (Attachment 9). The guidelines were

communicated to leases by Dear Operator/Payor letter of April 22, 1996 (Attachment 10).

The Board promulgated the coalbed gas guidelines in large part to address the $CO_2$-removal costs. Based on the regulations at 30 CFR § 206.158(d)(1), the Board concluded that no processing allowance may be claimed for extracting $CO_2$, unless the $CO_2$ is marketed and sold.[3] The Board further stated:

> From the data the coalbed methane producers submitted to MMS, it does not appear that (the $CO_2$ extraction) warrants an extraordinary processing allowance and the amine process is not extraordinary when compared to the kinds of processing in the overall industry. Therefore, under 30 CFR § 206.158(d)(2)(i), the costs of extracting the $CO_2$ from the methane generally would not appear to qualify for an extraordinary processing allowance and also should not be included in the transportation allowance allocated to the methane.

**Payor Handbook**

The *Oil and Gas Payor Handbook, Volume III*, which was written to explain more fully the intent and application of the valuation regulations, also provides guidance in this case. In addressing the marketable-condition regulations in 30 CFR § 206.158(d)(1), and specifically the clause regarding nonroyalty-bearing production, the handbook indicates that unsalable $CO_2$ is not royalty bearing and as such is not permitted a processing allowance (p. 7-2).

## EFFECT OF REGULATIONS

Processing allowances are applicable only against the value of gas plant products, unless MMS grants an extraordinary

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[3] The Board did note that the costs associated with $CO_2$ extraction may be claimed as processing allowance against the value of $CO_2$ to the extent the $CO_2$ is marketed and sold at a later date.

processing cost allowance (30 CFR § 206.158(c)(1)). The definition of "gas plant product" at 30 CFR § 206.151 is predicated on the product being marketable. Merriam-Webster's Collegiate Dictionary, Tenth Edition (1996), defines "marketable" as "fit to be offered for sale in a market," "wanted by purchasers or employers: SALABLE," and "of or relating to buying or selling."

At the outset it appears the extracted $CO_2$ does not qualify as a gas plant product because it is not marketable; it is vented because there is no market for it. Accordingly, $CO_2$ has no value against which to apply a processing allowance. Thus, the provisions of 30 CFR § 206.158(d)(1) addressing sweetening and nonroyalty production, in combination with 30 CFR §§ 206.158(b) and 206.158(c)(1), would appear to prohibit a processing allowance in this case. In view of the language in 30 CFR § 206.158(d)(2)(i) stating that extraordinary processing cost allowances are in addition to any other processing allowance to which the lessee is entitled, it would further appear that an extraordinary processing cost allowance is not warranted when a processing allowance is not applicable. In other words, because $CO_2$ in this case is not even eligible for a processing allowance, an extraordinary processing cost allowance is not proper.

Vastar points out, however, that MMS has granted an extraordinary processing cost allowance in a similar situation where $CO_2$ is vented and not marketed, referring to MMS's approval for Louisiana Land and Exploration Company's (LL&E) Lost Cabin Gas Plant (SOR at p. 4). Under 30 CFR § 206.158(d)(2)(i), the lessee must show that its costs are extraordinary, unusual, or unconventional by reference to standard industry conditions and practice to be eligible for an extraordinary processing cost allowance. The remainder of this report will show that Vastar's costs are not extraordinary, unusual, or unconventional.

## ARGUMENTS

1. Whether the composition of the gas stream is atypical when compared to conventional gas is subjective. Although composition will dictate the processes used to remove elements or compounds from a gas stream, composition by and of itself is not a sufficient criterion to grant an extraordinary processing cost allowance. *In fact, regulations provide that cost, not composition, is the determining factor in granting an extraordinary processing cost allowance.*

**Vastar's Position**

The main thrust of Vastar's arguments revolves around the composition of the coalbed gas entering the Val Verde Plant. Vastar contends this gas is "atypical" because it contains no liquid hydrocarbons and has a high $CO_2$ content. Thus, Vastar believes it satisfies the criteria for an extraordinary processing cost allowance as given in MMS's guidelines.[4] It argues that MMS erred in rejecting the gas as unusual for the following reasons (SOR for MMS-97-0191-O&G at p. 2):

- MSS ignores its own definition of "atypical" gas in Chapter 7.1.2 of the Oil and Gas Payor Handbook, Volume III, which states, "'Atypical' gas is defined as gas that does not contain liquefiable hydrocarbons, such as ethane, propane, butane, etc."
- MMS cited the lack of liquids as evidence supporting the extraordinary processing cost allowances granted

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[4] Vastar initially claimed in its allowance application that its coalbed gas is "unique," largely by reference to Exhibits 3 and 4 of Attachment 3. These exhibits were prepared by a group of coalbed gas producers in the San Juan Basin and presented to MMS for consideration in granting allowances. They are the same reports reviewed by the Royalty Policy Board in reaching its December 7, 1995, decision on coalbed gas valuation and reporting.

for LL&E's Lost Cabin Gas Plant and Exxon Corporation's LaBarge Gas Plant.

- Statistical evidence shows this gas to be compositionally noncomparable with other natural gas streams produced in the Lower 48 States.

**RVD's Position**

The composition of the gas stream alone does not automatically qualify a lessee for an extraordinary processing cost allowance. Under the regulations, cost is the ultimate allowance determinant. Gas composition is a factor in determining the eligibility for an extraordinary processing cost allowance primarily because composition will dictate in some manner the processing methods and plant design necessary to process the gas. Processing methods and plant design in turn effect costs.

As we discussed in our denial decisions (Attachment 2, p. 3 of Enclosure 1), natural gas exhibits a broad spectrum of compositions. We do not argue that Vastar's coalbed gas is distinguishable from non-coalbed gas, commonly referred to as "conventional" gas.[5] (We again note that Vastar does not submit its gas composition but instead refers to the composition of the commingled gas stream entering the Val Verde Plant. See footnote 1 for average gas compositions in Vastar's area of operations.) We do have a problem with classifying this gas as unique or atypical given the spectrum of gas compositions. Each gas stream has its own set of peculiarities that makes it different or distinguishable from another gas stream. Statistical analyses can be used to categorize gas streams by showing that certain hydrocarbon compositions or concentrations of impurities are more or less common than others. Based on the statistical

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[5] "Conventional" is a word commonly used to distinguish coalbed gas from other, non-coalbed gas streams. It has no formal meaning that we can find.

analysis presented in Vastar's SOR, the coalbed gas entering the Val Verde Plant is certainly distinguishable from other natural gas streams. But we don't agree that this distinction alone qualifies Vastar for an extraordinary processing cost allowance. Returning to 30 CFR § 206.158(d)(2)(i), it is the extraordinary, unusual, or unconventional cost of a processing operation that determines an extraordinary processing cost allowance.

The coalbed gas entering the Val Verde Plant is essentially dry gas; i.e., it contains negligible liquid hydrocarbons, with a relatively large amount of $CO_2$. However, the lack of liquid hydrocarbons as argued by Vastar, does not make it unusual or atypical. Dry gas production is neither atypical nor uncommon. For example, much of the "conventional" gas produced in central and northern Montana is dry gas. Furthermore, the definition of "atypical" on pa. 7-2 of the *Oil and Gas Payor Handbook, Volume III*, is not a formal one. Noteworthy here is the handbook's following sentence on p. 7-2, which instructs that the lessee must not only show the raw gas stream is atypical, but also the processing costs are extraordinary, unusual, or unconventional by reference to standard industry conditions and practice.

In summary, any argument that centers on gas composition to qualify for an extraordinary processing cost allowance is misplaced by being contrary to regulation.

2. *The amine process used to extract $CO_2$ at the Val Verde Plant is not extraordinary, unusual, or unconventional. It is widely used throughout the gas processing industry to remove acid gases.*

**Vastar's Position**

In its SOR for MMS-97-0063-O&G (p. 17), Vastar contends that the Val Verde Plant is more complex than conventional gas plants for the following reasons:

- The amine process used to extract CO2 uses a greater percentage of amine.

- The Val Verde Plant uses stainless steel in certain areas, rather than carbon steel.
- The Val Verde Plant requires larger amounts of water.

**RVD's Position**

As explained in our denial decision (Attachment 2, p. 4 of Enclosure 1), we do not view Val Verde's amine process as unconventional or extraordinary. We believe our analysis in that decision adequately supports our position. To both summarize and elaborate on that analysis:

- Amine solutions have been the generally accepted solvent to remove acid gases from natural gas streams. To our knowledge almost 80 percent of the gas plants in the United States use the amine process.
- Amine solutions are often specifically formulated and mixed with varying amounts of water to treat a given acid gas concentration. Besides the formulation used by Val Verde, there are at least eight other amine formulations, some more complex than others, available to the gas processing industry. The formulation used at Val Verde merely pushes the envelope of amine solutions.
- The principal design and equipment for the amine process (contactor towers, regeneration units, pipes, pumps, and controls) are much the same for both coalbed and conventional gas plants. In fact, Val Verde's amine trains 1 and 2 were purchased and used from an out-of-state, conventional gas treating facility and installed at their present location. The use of stainless steel is not uncommon when handling acid gases.
- The fact that the Val Verde Plant requires larger amounts of water is probably due in large part to its size and capacity. Val Verde consists of eight standalone treating plants, or "trains," with a total capacity

of 800 MMscf/d. Water is used in making up the amine solutions and rehydrating the methane. Vastar does not indicate the amount of water used on a unit basis or how this amount compares to other plants.

3. *Vastar does not demonstrate its unit costs to be extraordinary.*

**Vastar's Position**

In its SOR for MMS-97-0063-O&G (p. 17), Vastar claims its cost to remove $CO_2$ from the coalbed gas ($0.0778/Mcf) is significant.

**RVD's Position**

Under the regulations, cost is the ultimate determinant in granting an extraordinary processing cost allowance. Vastar does not offer any analysis to demonstrate that its cost is extraordinary, unusual, or unconventional by reference to standard industry conditions and practice, as required by 30 CFR § 206.158(d)(2)(i); it simply claims that its cost is significant.

As we indicated in our denial decision (Attachment 2, p. 5 of the Enclosure 1), Vastar's cost is considerably less than the costs for which MMS has previously granted extraordinary processing cost allowances. In fact, based on proprietary information submitted in support of other extraordinary processing cost allowance applications,[6] Vastar's cost at $0.0778/Mcf is at the law end of the range for $CO_2$-removal costs.

4. *The composition of the gas stream and processing techniques at Exxon Corporation's LaBarge Plant (118 IBLA 221, 1991) are distinguishable from those at the Val Verde Plant.*

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[6] We specifically refer to a proprietary report prepared for LL&E by Purvin & Gertz, Inc. MMS is not at liberty to release this report. Should Vastar wish to review this report, we recommend they contact LL&E directly for its release.

**Vastar's Opinions**

Vastar believes that Val Verde is in many ways compared to the LaBarge system at issue in *Exxon Corp.*, for which MMS has granted an extraordinary processing cost allowance. Claimed similarities include the high levels of $CO_2$ and lack of liquid hydrocarbons on both gas streams. (See SOR for MMS-97-0063-O&G at p. 17.) Vastar also contends the $CO_2$ removal process at Val Verde is, in some respects, more sophisticated than the process at LaBarge; where LaBarge uses a largely physical process to remove $CO_2$. Val Verde uses a chemical process.

**RVD's Commentary**

Any comparison with *Exxon Corp.* to support an extraordinary processing cost allowance would appear moot given that Vastar has not demonstrated its cost to be extraordinary, unusual, or unconventional. Nonetheless, we assert there are distinct differences between LaBarge and Val Verde, differences that would not support an extraordinary processing cost allowance for Val Verde.

As discussed above, any argument centering on gas composition to support an extraordinary processing cost allowance is misplaced; gas composition is not the sole, or even compelling, factor in granting such an allowance. We do not believe the lack of liquid hydrocarbons makes Vastar's gas necessarily atypical. As for $CO_2$, the gas entering the LaBarge Plant contains 65.4 percent $CO_2$, more than five times the amount of $CO_2$ entering the Val Verde Plant.

As for processing techniques, we've indicated that the basic amine process used at Val Verde is used by almost 80 percent of the gas plants in the United States, the primary difference being in the formulation of the amine solution. In contrast, the Selexol process used at LaBarge is, to our knowledge, used in only four other gas plants in the country.

Finally, and perhaps most important, a market exists for the $CO_2$ extracted at LaBarge. Thus, the $CO_2$ at LaBarge has value and is eligible for a processing allowance, making an extraordinary processing cost allowance proper in this case for the unrecovered costs of extracting $CO_2$.

5. *RVD's application denial is consistent with governing regulations.*

**Vastar's Allegation**

Vastar contends that RVD's application denial is so inconsistent with prior interpretation of the regulations and guidelines as to be arbitrary and capricious. Citing *U.S. Oil and Refining Co.*, 137 IBLA 223, 232 (1996) and *Union Oil Co. of California*, 116 IBLA 8, 16 (1990), Vastar alleges that RVD's decision is not supported by a rational basis.

**RVD's Commentary**

We did indeed analyze Vastar's application in review of the governing regulations (Attachment 2). We believe the rationale given in our decision, as well as our arguments given here, are consistent with the regulations.

The underlying thrust of Vastar's appeal appears to be a challenge to the Board's guidelines on coalbed gas valuation. The Board constructed those guidelines also in view of the regulations after lengthy deliberation. Our analysis and arguments given here support those guidelines.

## ADDITIONAL SUPPORT OF RVD'S POSITION

Although we have avoided the issue of marketable condition in this report, it is inherent in our arguments and explicitly raised as an issue in Vastar's SOR for MMS-97-0063-O&G (p. 9). IBLA has addressed a similar situation regarding the fees levied by a processor for sweetening sour gas in *Texaco Inc.*, 134 IBLA 109 (1995), only in this case the extracted contaminant was hydrogen sulfide instead of $CO_2$. The processor, Colorado Interstate Gas Company, charged Texaco $0.998/Mcf to sweeten Texaco's sour gas. MMS

disallowed a deduction for the sweetening costs on the grounds that such costs were for the purpose of making the production marketable. In deciding Texaco's appeal, IBLA concluded in pertinent part:

> A Federal oil and gas lessee's duty to put gas produced from the lease into a marketable condition includes sweetening sour gas by removing hydrogen sulfide, and the costs for such treatment are not deductible from the value of the production for royalty computation purposes no matter who performs the treatment or whether title to the gas passes before the sweetening occurs.

The Wyoming District Court affirmed IBLA's decision in *Texaco Inc. v. Quarterman* (96-CV-08-J, 1997).

This decision supports our position that Vastar's gas is ineligible for a processing allowance. It then follows that Vastar's gas is also ineligible for an extraordinary processing cost allowance. Vastar's costs compared to Texaco's are further evidence that an extraordinary processing cost allowance is not warranted in the instant case.

**SUMMATION**

Based on the foregoing, we submit that Vastar is not eligible for an extraordinary processing cost allowance for the following reasons:

1. Regulations at 30 CFR § 206.158(d)(1) prohibit a processing allowance when extracted products are not marketable. Accordingly, an extraordinary processing cost allowance is inappropriate under 30 CFR § 206.158(d)(2)(i).
2. Assuming, arguendo, that 30 CFR § 206.158(d)(2)(i) might permit an extraordinary processing cost allowance, Vastar has not demonstrated that its costs are extraordinary, unusual, or unconventional by comparison to standard industry conditions and practice.

We are sending a copy of this memorandum to Vastar. If you have any questions on this matter, please call Mr. Charles Brook at (303) 275-7250.

Attachments

## APPENDIX H

[Seal Omitted]

**United States Department of the Interior**

MINERALS MANAGEMENT SERVICE

Royalty Management Program
P.O. Box 25165
Denver, Colorado 80225-0165

MMS/SICD 7-4-10
MS 3660 93-60032.588

CERTIFIED MAIL –
RETURN RECEIPT REQUESTED May 27, 1997

Mr. Jim Shearrer
Supervisor, Audit Coordinator
Amoco Production Company
P.O. Box 591
Tulsa, Oklahoma 74102-0591

RECEIVED
June 10, 1997
Law Dept.
Denver, Colorado
Amoco Corporation

Dear Mr. Shearrer:

The New Mexico Taxation and Revenue Department (State), Oil and Gas Audit Section, has been delegated the authority by the Secretary of the Interior to perform audits and related investigations of Federal Oil and Gas leases located in New Mexico. This authority is in accordance with Section 205 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA). In this capacity the State has conducted a review of the Amoco Production Company (Amoco) policies regarding royalty calculations associated with sales of coalbed methane gas produced from Federal leases located in the San Juan Basin, New Mexico, during the period January 1, 1989, through December 31, 1996. The review was performed to determine whether additional royalties are due on coalbed methane proceeds associated with Federal leases. Our review disclosed that you have incorrectly calculated gross proceeds on these sales and as a

result, we have determined that additional royalties are due in the amount of $4,117,607.

Coalbed methane gas is produced from coal formations and as a result it has a higher content of carbon dioxide ($CO_2$). The content of the $CO_2$ can vary from minimal amounts to as much as 12 to 15 percent. In order to transport and sell the coalbed methane, the $CO_2$ level has to be reduced to around 2 to 3 percent. This requires that the coalbed methane be transported from the wellhead to a processing facility. Costs associated with the movement and processing of this gas include gathering, compression, dehydration and $CO_2$ removal. Producers are charged a fee by plant operators for performing these services. Based on our review, these charges were not considered by Amoco in determining the gross proceeds value for computing royalties.

The following discussion outlines the allowable as well as non-allowable deductions that may be utilized in the calculation of royalty value for coalbed methane.

Coalbed methane and associated products is valued in accordance with 30 CFR § 206.152 (1988). The value of coalbed methane is the gross proceeds accruing to the lessee under an arm's-length transaction for the sale of the gas including the costs of placing the gas in marketable condition. In the case of a non-arm's-length contract, value is determined based on the higher of gross proceeds or the valuation benchmarks at 30 CFR § 206.152(c). The value for royalty purposes also includes applicable allowances.

*Allowable Deductions:*

Transportation allowances are granted for the reasonable, actual necessary costs of transporting the coalbed methane from the royalty measurement point (either the well or the Central Delivery Point (CDP)) to the point of sale remote from the lease. The transportation allowance allocated to the coalbed methane should be calculated according to 30 CFR §§ 206.156 and 206.157 (1988). It may include the

costs of transporting the methane and the portion of the $CO_2$ permitted in the pipeline specifications. For example, if the pipeline specifications allowed 3 percent $CO_2$, the lessee will be allowed to include in the transportation allowance the costs of transporting 3 percent of the $CO_2$ volume.

Large quantities of water along with low quantities of gas are normally produced initially from coalbed methane wells. The resulting dehydration costs which occur prior to the royalty measurement point are not deductible. Dehydration costs occurring after the royalty measurement point are deductible as part of the transportation allowance.

Production from coalbed methane wells is enhanced by lowering wellhead pressure. Once produced, the pressure must be increased to move the gas down the line to the processing facility. The cost required to move coalbed methane would therefore be greater than normal because now additional compression is required to make up for the initial reduction in wellhead pressure utilized to enhance recovery. That portion of the compression costs incurred to enhance production of coalbed methane is not allowable. To the extent the producer can demonstrate that all or a portion of the compression costs are not necessary for enhanced recovery, that portion may be allowable as part of transportation.

In determining the transportation allowance for both arm's-length and non-arm's-length situations, the lessee has the burden to demonstrate what portion of the costs are attributable to transportation.

The costs of extracting the $CO_2$ cannot be included as part of a transportation allowance.

*Processing Allowance/Extraordinary Processing Allowances:*

Based on the regulations at 30 CFR § 206.158(d) (1) (1988), when gas is processed for the removal of acid gases, com-

monly referred to as sweetening, no processing cost deduction is allowed for such costs unless the acid gases removed are further processed into a gas plant product. Because the $CO_2$ is vented to the atmosphere, no processing allowance may be claimed for extracting the $CO_2$ from the coalbed methane. Based on data examined by the Minerals Management Service (MMS), the costs of extracting the $CO_2$ from the coalbed methane do not qualify for an extraordinary processing allowance.

*Other Non-allowable Deductions:*

Gathering from the wellhead to the CDP when the Bureau of Land Management has approved the CDP as the point of royalty settlement is not an allowable deduction.

Wellhead separation costs are not an allowable deduction from the value of the coalbed methane.

The State sent Amoco an Issue letter dated November 16, 1995, that identified two issues relating to the San Juan 30-6 Unit coalbed methane Agreement #891-000538-A. The Issues were 1) under-reported volumes for the Agreement and 2) the methodology used to value the gas produced from the Agreement.

*Pricing Methodology:*

Burlington Resources/Meridian Oil Inc. is the operator of the San Juan 30-6 Unit for Agreement #891-000538-A. Most of the gas is gathered and transported on a system owned by Meridian's affiliate, Meridian Oil Gathering Inc. (MOGI) commonly referred to as the Val Verde System. This system is designed to transport coalbed methane gas to their processing facility and then to the El Paso Natural Gas mainline transportation system. MOGI's processing facility is used strictly to separate the $CO_2$ and make the gas marketable. In Amoco's reporting on their leases, the price reported is net of deductions taken for gathering, treating and removal of the $CO_2$ from the gas stream.

In 1995 producers in the San Juan Basin of New Mexico that produce coalbed methane gas, requested MMS to consider allowing certain costs as a transportation allowance or as an extraordinary processing costs to be deductions from the value of the methane. By letter dated December 7, 1995, the Royalty Policy Board (RPB) issued the Coalbed Methane Valuation and Reporting Guidelines as outlined above. The RPB disallowed the costs to remove the $CO_2$ from the gas stream and disallowed the cost to transport the $CO_2$ volumes to the processing or treating facility, with an adjustment for the amount of $CO_2$ allowed by the major pipeline transporters.

The State has applied the regulations and guidelines in the MMS/RPB letter of December 7, 1995, to calculate the royalties for the San Juan 30-6 Unit as follows:

> By letter dated December 19, 1995, the State requested Amoco to provide a breakdown of costs associated with transporting the coalbed methane to a processing plant. Amoco's response was based on information received from Meridian by letter dated May 29, 1996, that indicated a cost of the $CO_2$ removal to be $0.778 per MCF.

The State applied the following regulations, guidance and decisions to determine the allowable transportation rate that is applied only to the royalty bearing portion of the-full gas stream collected at the CDP's. The transportation allowance allocated to the coalbed methane gas must be calculated in accordance with 30 CFR §§ 206.156 and 206.157 (1988).

30 CFR § 206.157(2) (i) states:

> If an arm's-length transportation contract includes more than one product in a gaseous phase and the transportation costs attributable to each product cannot be determined from the contract, the total transportation cost shall be allocated in a consistent and

> equitable manner to each of the products transported in the same proportion as the ratio of the volume of each product (excluding waste products which have no value) to the volume of all products in the gaseous phase (excluding waste products which have no value). Except as provided in this paragraph, *no allowance may be taken for the costs of transporting lease production which is not royalty bearing without MMS approval.* [Emphasis added.]

The State broke the costs into two parts, disallowed $CO_2$ removal, and disallowed transportation of $CO_2$. The disallowed $CO_2$ removal rate is calculated by multiplying Amoco's total unit volumes by the $.0778 per MCF rate indicated in the Meridian letter as the cost to remove the $CO_2$ at the Val Verde Plant. The disallowed transportation of the $CO_2$ is calculated by taking Amoco's total unit volumes by the $CO_2$ percentage in the gas stream adjusted for the $CO_2$ percent allowed by the major pipeline transporters (2 percentage was used in this audit). The volume is then multiplied by the transportation portion in the contract rate to transport the $CO_2$ volumes from the field (CDP) to the processing facility. The $CO_2$ percentage used in these calculations is the percentage of $CO_2$ at the inlet of the Val Verde Plant, as provided by Meridian, ranging from 10.8000% in December 1988 to 12.2000% for December 1995 as shown on Schedule F. The Transportation rate used from January 1989 through October 1990 is ($.395 - $.0778 = $.31720). From November 1990 through December 1996 the rate is ($.3600 - $.0778 = $.2822). The State was provided with Unit total Volumes from January 1992 through December 1996. The State has calculated Amoco's royalties through December 1996 for the San Juan 30-6 in the amount of $432,158 (Schedule A).

Amoco is a working interest owner and lessee in the Northeast Blanco Unit (NEBU) that is operated by Blackwood Nichols (BN). Through an arrangement with the working

interest owners in the unit, BN reported and paid royalties on Amoco's behalf. On July 9, 1996, the State sent BN a letter regarding the NEBU coalbed methane gas issue. The letter also addressed the interest of Amoco and the other working interest for which BN reported and paid royalties. By letter dated September 3, 1996, Amoco requested that the findings relating to the NEBU on coalbed methane gas be addressed directly to Amoco. By letter dated September 9, 1996, the State notified Amoco the NEBU would be combined with all of Amoco's coalbed gas issues in the San Juan Basin.

On October 15, 1996, the State received a response from Amoco. The letter stated that the removal of $CO_2$ from coalbed gas should be permitted as a transportation expense or extraordinary processing costs. The letter further stated that MMS should grant an alternative method of valuation from coalbed gas produced from Federal lands. These comments have been incorporated into the body of this letter, along with responses. Our audit addresses the issue using regulations in effect at the time of the gas production subsequent interpretation by MMS.

The State's audit of the NEBU covered the period May 1990 through December 1993. For this period, Amoco's coalbed gas sales from the NEBU and other San Juan Basin leases (except the San Juan 30-6) was going to Williams Field Services. By letter dated May 20, 1996, the State requested Amoco to provide copies of transportation and treating contracts for the period January 1989 through December 1995 from Meridian on the Val Verde System, and from Williams for the period July 1992 through December 1995 for the Milagro and Manzanares Systems. The State also requested Amoco to provide the volumes going through each system for this 1989 through 1995 period. Amoco provided Contract #143-063 – *Discounted Coal Seam Gathering, Treating, and Transportation Rates*

*and Purchase Obligation* dated June 15, 1990, and Letter Agreement dated February 13, 1990. Amoco and Conoco entered into this agreement with Williams for the purpose of Northwest/Williams to purchase, gather, treat and/or transport Amoco's and/or Conoco's coalseam gas on an interim basis and the construction and operation of certain new Williams facilities (Trunk S – Manzanares & Milagro Treating Facility) for the purpose of gathering, dehydrating, treating and transporting coalseam gas from the 30-8 area and the NEBU in the San Juan Basin of New Mexico on to El Paso Natural Gas Company mainline near Bloomfield, New Mexico. The rate for service for gas processed by Williams Ignacio Plant in Colorado is $.30/MCF. The components of this rate are $.1353/MCF for gathering, *$.0795/MCF for treating*, and $.0852/MCF for transportation. This rate is used for the period February 1990 through June 1992 for all of Amoco's coalseam gas going through Ignacio. Williams, in a letter to producers dated May 1, 1996, indicated that 21% of their contract rate for the Manzanares System is for treating and removal of $CO_2$ and the balance is for transportation.

From July 1992 to December 1995, Amoco provided schedules of their coalbed methane gas going through Williams new Manzanares and Milagro Treating Facility. For the NEBU, Amoco indicated that Williams was charging the following rates for each CDP: Sims $.26, Pump $.30, and Middle $.30. Amoco also provided the State with $CO_2$ percentages for the test months for each property. Amoco indicated that some gas from the NEBU went to Meridian's Val Verde Plant during this period. The State re-calculated royalties for the NEBU for the period January 1990 through December 1995 using the volumes for each transportation system as provided by BN and Amoco. For volumes going through Ignacio and Milagro, the State used the $CO_2$ percentage at the CDP's as provided by BN. For volumes going through Val Verde, the State used the $CO_2$

percentages at the Plant inlet as provide by Meridian. The State calculated additional royalties due for the disallowed cost of removal of the $CO_2$ and the transportation of the $CO_2$ volumes for the NEBU for the period January 1990 through December 1995 in the amount of $1,308,372 (Schedule D).

For Amoco's other coalbed methane volumes going through the Manzanares System, the State calculated the disallowed costs for the period July 1992 through December 1995, using the volumes provided by Amoco and the $CO_2$ percentage at each meter as provided by Amoco. The $CO_2$ percentage has been adjusted for a 2% allowable by the mainline pipeline transporter. The State calculated additional royalties in the amount of $2,170,962 (Schedule C).

For Amoco's coalbed methane volumes (other than San Juan 30-6 and NEBU) going through the Val Verde Plant, the State used the volumes provided by Amoco, the treating and removal rates as provided by Coopers and LyBrand, and used the $CO_2$ percentage at the Plant inlet as adjusted for 2% as provided by Meridian. The State calculated additional royalties due for the period October 1992 through December 1995 or $206,115 (Schedule C-1).

The value used by Amoco in its royalty calculations included volumes which had been reduced by non-allowable deductions. Amoco's failure to calculate gross proceeds utilizing only allowable deductions as noted above has resulted in an underpayment of royalties. Therefore, in order to bring royalty payments into compliance with the aforementioned regulations and decisions, Amoco is directed to pay additional royalties of $4,117,607 as presented in the attached schedules. *Payment must be mailed to the address indicated on the enclosed bill, and must be made payable to the U.S. Department of the Interior, MMS and must be received by the invoice date.* To ensure proper credit to your account, please include your payment and the remit-

tance copy of the bill for collection. In order to simplify the billing process, MMS has calculated and accumulated royalty underpayments into Federal Lease No. 029-012293-0. However, Amoco will still be required to submit separate lines of Form MMS-2014 for each lease and sales month. Your payment should be tendered in accordance with the regulations at 30 CFR § 218.51 (1996) and accompanied by an appropriately completed *green* Form MMS-2014 (forms and instructions enclosed) using adjustment reason code *40*. The green form MMS-2014 must reflect *650118* in block *3a* "Payor Assigned Document Number."

The State has identified a consistent and systemic error in the reporting and paying of royalties from the various leases in the San Juan Basin of New Mexico. Therefore, Amoco is ordered to perform the following compliance actions within 90 days of receipt of this letter:

1. Identify any other Federal and Indian leases not included above, for which Amoco is the responsible payor or lessee, and where coalbed methane is produced in the San Juan Basin.
2. For all leases identified in (1), re-calculate and pay the additional royalties due in accordance with the guidelines outlined above for all periods from January 1989 through August 1996. (If you are unable to identify and segregate the various costs in order to insure that only allowable costs have been deducted in arriving at the proper value for royalties, then the MMS will assist you in determining the allowable deductions.)
3. For all leases included in the attached schedules (other than San Juan 30-6), re-calculate and pay the additional royalties due in accordance with the guidelines outlined above for all periods from January 1996 through August 1996.
4. All supporting calculations and source documents are subject to audit by MMS, therefore, should be re-

tained by Amoco until MMS completes its follow-up compliance testing.

Appropriate late payment charges pursuant to 30 CFR § 218.102 (1996) will be computed and billed to Amoco upon receipt of payment of the additional royalties due.

Royalty calculations subsequent to the current production month must also be in compliance with regulatory determination referred to in this order. If in the future, we determine that the required recomputations have not been performed and future royalty payments do not comply with this order, the violations may be considered willful.

A copy of your payment and green Form MMS-2014 should be sent to:

Mr. Jay Norman, Supervisor
Taxation and Revenue Department
Oil and Gas Audit Section
Manuel Lujan Building
1200 South St. Francis Drive
Santa Fe, New Mexico 87509

Section 109 of FOGRMA, promulgated in 30 CFR § 241.51 (1996), authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, or permit. Consequently, your failure to comply with the terms of this order may be considered a violation pursuant to 30 CFR § 241.51, and could subject you to penalties of up to $5,000 per violation per day for each day such violation continues and up to $10,000 per violation each day if the violation is considered to be willful.

You have the right to appeal in accordance with the provi

sions of 30 CFR Part 290 (1996). Any appeal taken will be to the Director, MMS, and the notice of appeal must be filed within 30 days from the date of receipt of this order with:

Mr. James R. Detlefs, Chief
Minerals Management Service
State and Indian Compliance Division
P.O. Box 25165, MS 3660
Denver, Colorado 80225-0165

Any notice of appeal shall incorporate or provide by separate letter written statements of reasons, as you deem adequate, to justify reversal or modification of this directive. You have 60 days from receipt of this letter to file any statements of reasons or written brief to explain your appeal. This filing requirement runs concurrent with the requirement to file the appeal. If the filing requirement for statements of reasons cannot be fulfilled within 60 days of the receipt of the order, an extension of time to file statements of reasons must be obtained. Time extensions for filing the statements of reasons will not be authorized unless requested in writing with justification showing good cause for the time extension. Further, the written request for the time extension must be provided to the Division Chief at the address shown above for approval.

In accordance with the provisions of 30 CFR § 243.2 (1996), compliance with order will be suspended upon the posting of an adequate surety pending the outcome of the appeal. The surety must be received at MMS by the due date. The surety must be in the amount of $5,959,300 which includes the principal plus interest that will accrue through March 31, 1998. Upon request by MMS, the amount of the surety will be increased periodically, if necessary, to cover any additional interest that may accrue. Enclosed are instructions for posting the surety.

If you have any questions, please contact Mr. Jay Norman of the State at (505) 827-0986, or Ms. Carol Green of MMS at (303) 275-7459.

Sincerely,

/s/ James R. Detlefs
James R. Detlefs
Chief, State and Indian
Compliance Division

8 Enclosures

cc: Mr. Jay Norman
Taxation & Revenue Department
Oil and Gas Audit Section
Manual Lujan Building
1200 South St. Francis Drive
Santa Fe, New Mexico 87502

## APPENDIX I

[Seal Omitted]

**United States Department of the Interior**

MINERALS MANAGEMENT SERVICE

Royalty Management Program
P.O. Box 25165
Denver, Colorado 80225-0165

January 22, 1997

MMS/SICD 7-11-22
MS 3660

3-40001.562

Received /28/97

CERTIFIED MAIL --
RETURN RECEIPT REQUESTED

Mrs. Mary Holman
PRC-C5128
The Atlantic Richfield Company
2300 West Plano Parkway
Plano, Texas 75075

Re: Royalties on Coalbed Methane Agreement #891-000538-A

Dear Mrs. Holman:

The New Mexico Taxation and Revenue Department's (State), Oil and Gas Audit Section has been delegated the authority by the Secretary of the Interior to perform audits and related investigations of Federal Oil and Gas leases located in New Mexico. This authority is in accordance with Section 205 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA). In this capacity the State has conducted a review of The Atlantic Richfield Company (ARCO), regarding royalty calculation policies associated with sales of coalbed methane gas produced from Federal leases located in the San Juan Basin of New Mexico,

specifically the San Juan 30-6 Unit, located in Rio Arriba County. The review was performed to determine whether additional royalties are due on coalbed methane proceeds associated with Federal leases. Our review disclosed that you have incorrectly calculated gross proceeds on these sales and as a result, we have determined that additional royalties are due.

Coalbed methane gas is produced from coal formations and as a result it has a higher content of carbon dioxide ($CO_2$). The content of the $CO_2$ can vary from minimal amounts to as much as 12 to 15 percent. In order to transport and sell the coalbed methane, the $CO_2$ level has to be reduced to around 2 to 3 percent. This requires that the coalbed methane be transported from the wellhead to a processing facility. Costs associated with the movement and processing of this gas include gathering, compression, dehydration and $CO_2$ removal. Producers are charged a fee by plant operators for performing these services. Based on our review, these charges were not considered by ARCO in determining the gross proceeds value for computing royalties.

The following discussion outlines the allowable as well as the non-allowable deductions that may be utilized in the calculation of royalty value for coalbed methane.

Coalbed methane and associated products should be valued in accordance with 30 CFR §206.152 (1988). The value of coalbed methane is the gross proceeds accruing to the lessee under an arm's-length transaction for the sale of the gas including the costs of placing the gas in marketable condition. In the case of a non-arm's-length contract value is determined based on the higher of gross proceeds or the valuation benchmarks at 30 CFR §206.152(c). The value for royalty purposes also includes applicable allowances.

*Allowable Deductions*:

Transportation allowances are granted for the reasonable, actual necessary costs of transporting the coalbed methane

from the royalty measurement point (either the well or the Central Delivery Point (CDP)) to the point of sale remote from the lease. The transportation allowance allocated to the coalbed methane should be calculated according to 30 CFR §§ 206.156 and 206.157 (1988). It may include the costs of transporting the methane and the portion of the $CO_2$ permitted in the pipeline specifications. For example, if the pipeline specifications allowed 3 percent $CO_2$, the lessee will be allowed to include in the transportation allowance the costs of transporting 3 percent of the $CO_2$ volume.

Large quantities of water along with low quantities of gas are normally produced initially from coalbed methane wells. The resulting dehydration costs which occur prior to the royalty measurement point are not deductible. Dehydration costs occurring after the royalty measurement point are deductible as part of the transportation allowance.

Production from coalbed methane wells is enhanced by lowering wellhead pressure. Once produced, the pressure must be increased to move the gas down the line to the processing facility. The cost required to move coalbed methane would therefore be greater than normal because now additional compression is required to make up for the initial reduction in wellhead pressure utilized to enhance recovery. That portion of the compression costs incurred to enhance production of coalbed methane is not allowable. To the extent the producer can demonstrate that all or a portion of the compression costs are not necessary for enhanced recovery, that portion may be allowable as part of transportation.

In determining the transportation allowance for both arm's-length and non-arm's-length situations, the lessee has the burden to demonstrate what portion of the costs are attributable to transportation.

The costs of extracting the $CO_2$ cannot be included as part of a transportation allowance.

*Processing Allowances/Extraordinary Processing Allowances:*

Based on the regulations at 30 CFR § 206.158(d) (1) (1988), when gas is processed for the removal of acid gases, commonly referred to as sweetening, no processing cost deduction is allowed for such costs unless the acid gases removed are further processed into a gas plant product. Because the $CO_2$ is vented to the atmosphere, no processing allowance may be claimed for extracting the $CO_2$ from the coalbed methane. Based on data examined by the Minerals Management Service (MMS), the costs of extracting the $CO_2$ from the coalbed methane do not qualify for an extraordinary processing allowance.

*Other Non-allowable Deductions:*

Gathering from the wellhead to the CDP when the Bureau of Land Management (BLM) has approved the CDP as the point of royalty settlement is not an allowable deduction.

Wellhead separation costs are not an allowable deduction from the value of the coalbed methane.

At the request of the Farmington, New Mexico office of the BLM, the State performed an audit of the San Juan 30-6 Unit for the period January 1, 1989, through December 31, 1991. The BLM had identified that volumes were not being reported correctly for Agreement #891-000538-A. All production from this Agreement is coalbed methane gas. During the audit period there were 19 different revisions to this Agreement (revisions 12 through 30). The thirtieth revision was approved in October 1993 with an effective date of July 1, 1991. The State's review of transporter statements from El Paso Natural Gas (EPNG) and from Northwest Pipeline (NWPL)/Williams Field Services (WFS) indicated that 217,310,320 MCF had been trans-

ported from the unit wells for this audit period. The State confirmed BLM's position that 100 percent of the unit production was not being reported on Forms MMS-2014. According to MMS, ARCO is a royalty payor and lessee for the following leases under this Agreement. Tract 25 Lease #029-003385-0, Tract 26 Lease #029-003403-0, Tract 12 Lease #082-080711-0, and Tract 15 Lease #082-080712-0. All the above leases were included in revisions 12 through 30 for the audit period. The State determined that an entitlement basis should be used to bring the unit leases into compliance because this was the method used by all working interest owners in the unit.

The Oil and Gas Payor Handbook under "Allocating and Reporting Sales from Leases and Agreements" states:

> On Federal and Indian leases having an initial unit or Communitization Agreement pending, royalties should be reported and paid on 100% of sales under current lease terms until such time as the Agreement is approved. If the Agreement is approved, retroactive reporting adjustments will be required to accurately reflect allocations specified in the new Agreement.

Royalties must be based on the most current Agreement allocation schedule approved by BLM or MMS, regardless of whether the quantity allocated to the lease is less than, equal to or greater than the quantity actually sold on the lease. This accounting is compelled by language generally involved in unit and Communitization Agreements:

> All unitized/communitized substances produced from each participating area established under this Agreement, . . . shall be deemed to be produced equally on an acreage basis from the several tracts of unitized/communitized land of the participating area established for such production and, for the purpose of determining any benefits accruing under this

> Agreement, each tract of unitized/communitized land shall have allocated to it such percentage of said production as the number of acres of such tract included in said participating area bears to the total acres of unitized/communitized land in such participating area . . .

The Federal Regulations at 30 CFR § 202.150(e) (1) (1988) entitled "Royalty on Gas" stated, in part:

> . . . In those instances where the lessee of any lease committed to a Federally approved unitization or Communitization Agreement does not actually take the proportionate share of the production attributable to its Federal or Indian lease under the terms of the Agreement, the full share of production attributable to the lease under the terms of the Agreement nonetheless is subject to the royalty payment and reporting requirements of this title.

Using this methodology for each unit tract for each of the nineteen revisions the State has calculated ARCO's entitled volumes for the period January 1989 through June 1996, to be 61,866,726 MCF. By comparing this volume to the volumes reported on the Form MMS-2014 for ARCO's four leases, ARCO had underreported volumes of 1,402 MCF, however, by using the ARCO reported prices as reported on the Form MMS 2014 for these entitled volumes it appears that ARCO over-reported royalties by $45,742 (Schedule A).

Meridian Oil Inc. (MOI) is the operator of the San Juan 30-6 Unit for Agreement #891-000538-A. Most of the gas is gathered and transported on a system owned by Meridian's affiliate, Meridian Oil Gathering Inc. (MOGI) commonly referred to as the Val Verde System. This system is designed to transport coalbed methane gas to their processing facility and then to EPNG's mainline transportation

system. MOGI's processing facility is used strictly to separate the $CO_2$ and make the gas marketable.

For the period January 1989 through March 1992, ARCO was selling all their production to Meridian under the joint operating agreement. Since March 1992, ARCO has marketed their production under various selling arrangements.

During the period January 1989 through March 1992, ARCO's price received from Meridian was based on a sale at the wellhead to Meridian's affiliate, Meridian Oil Trading Inc. (MOTI). Based on third party information, the State has determined that the wellhead prices offered by Meridian were reduced by costs associated with transporting the gas, and the processing to remove the $CO_2$ from the gas stream.

The regulations at 30 CFR § 206.152(i) (1988), state, in part:

> The lessee is required to place gas in marketable condition at no cost to the Federal Government . . . unless otherwise provided in the lease agreement. Where the value established pursuant to this section is determined by the lessee's gross proceeds, that value shall be increased to the extent that the gross proceeds have been reduced because the purchaser . . . is providing certain services, the cost of which ordinarily is the responsibility of the lessee to place the gas in marketable condition.

The State has applied the regulations and guidelines in the MMS Royalty Policy Committee letter of December 7, 1995, to calculate the royalties for the San Juan 30-6 Unit as follows:

> On January 8, 1996, the State requested ARCO to provide a breakdown of costs associated with transporting the coalbed methane gas to the processing plant, any costs of dehydration prior to the CDP and after the CDP, any costs associated with compression

> incurred to enhance production, or any compression necessary to move the gas to the processing plant, and costs associated with the removal of the $CO_2$ from the gas stream. ARCO's response to the State's request, was based on information received from Meridian by letter dated May 29, 1996, stated the cost of the $CO_2$ removal was $.0778 per MCF.

The State calculated the transportation rate and the processing rate based on the December 7, 1995, letter and the regulations. The State applied the following regulations, guidance and decisions to determine the allowable transportation rate that is applied only to the royalty-bearing portion of the full gas stream collected at the CDP's. The transportation allowance allocated to the coalbed methane gas must be calculated in accordance with 30 CFR §§ 206.156 and 206.157 (1988). 30 CFR § 206.157(2)(i) states:

> If an arm's-length transportation contract includes more than one product in a gaseous phase and the transportation cost attributable to each product cannot be determined from the contract, the total transportation cost shall be allocated in a consistent and equitable manner to each of the products transported in the same proportion as the ratio of the volume of each product (excluding waste products which have no value) to the volume of all products in the gaseous phase (excluding waste products which have no value). Except as provided in this paragraph, *no allowance may be taken for the costs of transporting lease production which is not royalty bearing without MMS approval.* [Emphasis added.]

The State broke the costs into two parts: disallowed $CO_2$ removal, and disallowed transportation of $CO_2$. The disallowed $CO_2$ removal rate is the total rate used to extract enough $CO_2$ from the methane to meet pipeline contract requirements (2% was used in this audit), called the pro-

cessing rate. The disallowed transportation of $CO_2$ is the cost in the contract rate used to transport $CO_2$ volumes from the field (CDP) to the processing facility. The actual rate used by ARCO varied most months after April 1992. Schedule C calculates the actual rate used by the company and this number is used in the calculation in Schedule B. The $CO_2$ percentage used in these calculations is the percentage of $CO_2$ at the inlet of the Val Verde plant, as provided by Meridian, ranging from 10.8000% in December 1988 to 12.2000% for December 1995 as shown on Schedule D.

ARCO sent a response to the State dated September 19, 1996, in reference to the coalbed methane cost issue. They provided schedules for the San Juan 30-6 Unit leases for the period October 1989 through the month of June 1996 which indicated additional royalties due of $556,558.96. However, their schedules were calculated for just the $CO_2$ removal using the $.0778 treating rate with no calculation for the transportation adjustment, plus an adjustment for an overpayment of royalties for the period of $117,349.56. This overpayment was arrived at using a different price than that originally reported on the Form MMS-2014. The State has recalculated the $CO_2$ removal cost beginning with January 1989 and using ARCO's volumes for periods after January 1992. This calculation indicates that additional royalties are due of $601,432 (Schedule B).

The disallowed transportation amount was calculated using the entitled volumes times the average $CO_2$ content as provided by Meridian, allowing for the 2% pipeline quantity, to arrive at the disallowed transported volumes. We then multiplied these volumes by the difference in the total contract rate and the $CO_2$ removal rate. For periods January 1989 through October 1990 the rate was $.395 per MCF, for the period from November 1990 through March 1992 the rate was $.36 per MCF, and for the time period April 1992 through June 1996 the rate varied as shown in Schedule B.

This resulted in additional royalties of $226,683 (Schedule B).

In order to bring royalty payments into compliance with the aforementioned regulations and decisions, ARCO is directed to pay additional royalties of $782,373 as presented in the enclosures ($601,432 + $226,683 - $45,742). *Payment must be mailed to the address indicated on the enclosed bill, and must be made payable to the U.S. Department of the Interior, MMS and must be received by the invoice date.* To ensure proper credit to your account, please include your payment and the remittance copy of the bill for collection. In order to simplify the billing process, MMS has calculated and accumulated royalty underpayments into Federal Lease No. 029-003385-0. However, ARCO will still be required to submit separate lines on Form MMS-2014 for each lease and sales month. Your payment should be tendered in accordance with the regulations at 30 CFR § 218.51 (1996) and accompanied by an appropriately completed ***green*** Form MMS-2014 (forms and instructions enclosed) using adjustment reason code ***40***. The green Form MMS-2014 must reflect ***752179*** in block 3a "Payor-Assigned Document Number."

The State has identified a consistent and systemic error in the reporting and paying of royalties on the various leases located in the San Juan 30-6 Unit in the San Juan Basin. Therefore, ARCO is directed to perform the following:

1. For the period January 1989 through August 1996, recalculate the royalties for all other coalbed methane Federal and Indian leases in the San Juan Basin that have been transported and processed through the Val Verde System, and the price has been reduced for the costs of the transportation and removal of the $CO_2$ from the gas stream. Include in the calculation all non-operated Federal and Indian leases, where

ARCO takes their gas in-kind, and sells the gas arm's length to MOTI or any other purchaser.

2. If ARCO's royalty redetermination indicates additional royalties are due, all payments must be made within 90 days of receipt of this letter. Your payments and Form MMS-2014 must be completed in accordance with the instructions indicated above.

3. All supporting calculations and source documents are subject to audit by MMS, therefore, should be retained by ARCO until MMS completes its followup compliance testing.

Appropriate late payment charges pursuant to 30 CFR § 218.102 (1996) will be computed and billed to ARCO upon receipt of payment of the additional royalties due.

Royalty calculations subsequent to the current production month must also be in compliance with regulatory determination referred to in this order. If in the future, we determine that the required recomputations have not been performed and future royalty payments do not comply with this order, the violation may be considered willful.

A copy of your payment and green Form MMS-2014 should be sent to:

Mr. Jay Norman
New Mexico Taxation and Revenue Department
Oil and Gas Audit/Compliance Section
1200 South St. Francis Drive
Santa Fe, New Mexico 87502

Section 109 of FOGRMA, promulgated at 30 CFR § 241.51 (1996), authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. Consequently, your failure to comply with the terms of this order may be considered a violation pursuant to 30 CFR § 241.51 and could subject you to penalties of up to $5,000

per violation for each day such violation continues and up to $10,000 per violation for each day if the violation is considered to be willful.

You have the right to appeal in accordance with the provisions of 30 CFR Part 290 (1996) and the Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 (Public Law 104-185, 110 Statute 1700). Any appeal taken will be to the Director, MMS, and the notice of appeal must be filed within 30 days from the date of receipt of this order with:

Mr. James R. Detlefs, Chief
State and Indian Compliance Division
Minerals Management Service
P.O. Box 25165, Mail Stop 3660
Denver, Colorado 80225-0165

Any notice of appeal must be accompanied by a written statement of reasons, as you deem adequate, to justify removal or modification of this order. Within 60 days from receipt of this order, the appellant will be permitted to file additional statements of reasons or written briefs. However, you must state in your initial notice of appeal to MMS your intention to submit additional statements of reasons. Extensions for filing the statement of reasons will not be permitted unless requested in writing by the appellant within the 30-day period allowed for filing the appeal with justification showing good cause for the time extension.

In accordance with the provisions of 30 CFR § 243.2 (1996), compliance with this order will be suspended upon the posting of an adequate surety pending the outcome of the appeal. The surety must be received at MMS by the due date. The surety must be in the amount of $1,265,100 which includes the principal plus interest that will accrue through January 31, 1998. Upon request by MMS, the amount of the surety will be increased periodically, if necessary, to

cover any additional interest that may accrue. Enclosed are instructions for posting the surety.

If you have any questions, please contact Mr. Jay Norman of the New Mexico Taxation and Revenue Department at (505) 827-0986 or Ms. Carol Green of MMS at (303) 275-7459.

Sincerely,

//James R. Detlefs//
James R. Detlefs
Chief, State and Indian
Compliance Division

7 Enclosures

## APPENDIX J

[Seal Omitted]

# United States Department of the Interior

MINERALS MANAGEMENT SERVICE

Royalty Management Program
P.O. Box 25165
Denver, Colorado 80225-0165

April 22, 1996

Dear Operator/Payor:

The Minerals Management Service (MMS) has received many questions, primarily from producers in the vicinity of New Mexico's San Juan Basin, on how to report and pay royalties on coalbed methane. The following guidelines answer those questions.

These guidelines apply to coalbed methane produced from Federal and Indian leases. You must follow these guidelines to ensure proper payment of royalties and correct reporting of production. They apply specifically to circumstances where carbon dioxide ($CO_2$) is removed from produced coalbed methane and is vented without sale.

### Valuing Production

*Sales at the wellhead or CDP*

If you sell your coalbed methane at the wellhead or a central delivery point (CDP) in the field or unit, you must value the coalbed methane as unprocessed gas under 30 CFR § 206.152 (1995).

For arm's-length sales, value for royalty purposes will be the gross proceeds you receive under your arm's length contract. However, that value cannot be reduced, either directly or indirectly, for the costs of placing coalbed methane in marketable condition. Placing production in marketable condition includes, but is not limited to, $CO_2$ removal (commonly called sweetening). Under 30 CFR § 206.152(I), if your sales price is reduced by fees for

services to place production in marketable condition, either directly or indirectly, you must add that portion of the fees attributable to those services, including $CO_2$ removal, to your gross proceeds received from the sale of the coalbed methane to determine value for royalty purposes. If you pay a bundled fee for both $CO_2$ removal and transportation, we recognize that you may be unable to obtain the information necessary to segregate the $CO_2$-removal costs. If you are in this situation, contact the MMS' Valuation and Standards Division at 303-275-7240 for assistance in determining the portion of your service fees attributable to $CO_2$ removal.

For non-arm's-length sales, you must determine the value of the coalbed methane under the methods (benchmarks) described at 30 CFR § 206.152(c). Again, you cannot deduct costs of placing the coalbed methane in marketable condition. You must ensure that any value determined under the methods is not improperly adjusted for nonallowable costs.

For Indian leases, you must also meet the dual accounting and majority price requirement established by regulation and lease terms. However, for both Federal and Indian leases, under no circumstances can the value of the production for royalty purposes be less than the gross proceeds accruing to the lessee, less applicable allowances.

*Sales at the $CO_2$-removal facility*

If you sell your coalbed methane at the tailgate of a $CO_2$-removal or other treating facility, you must value it as unprocessed gas under 30 CFR § 206.152. For arm's-length sales, value will be your gross proceeds under the arm's-length contract. For non-arm's-length sales, you must determine the value of the coalbed methane under the benchmarks at 30 CFR § 206.152(c). You cannot deduct costs of removing the $CO_2$ or otherwise placing the coalbed methane in marketable condition. However, you can deduct costs of transportation as discussed below.

**Determining Allowable Deductions From value**

*Transportation allowances*

You can take a transportation allowance for your reasonable, actual, and necessary costs of transporting the coalbed methane from the royalty measurement point (either the wellhead or the CDP) to the point of sale remote from the lease. You must use the regulation in 30 CFR § 206.156 and 206.157 (1995) and the instructions in Chapter 6 of the *Oil and Gas Payor Handbook, Volume III*, to calculate your transportation allowance.

In general, the regulations state that (1) you must allocate your transportation charges to all products produced and transported, and (2) you can only deduct the allocated costs from the value of products that are royalty bearing. For coalbed methane production, you can increase the transportation costs allocated to the methane component for the amount of $CO_2$ permitted in the main (inter- or intrastate) transmission line. For example, if your gas stream consists of 90 percent methane and 10 percent $CO_2$ and the main transmission line allows 2 percent $CO_2$ in the makeup of its gas stream, you can include the costs of transporting the 2 percent $CO_2$ volume (or 92 percent of the total transportation cost) when calculating your allowance for methane.

You can include costs of dehydration occurring after metering at the royalty measurement point in your transportation allowance but you cannot deduct costs of dehydration occurring at the wellhead. You can include costs for compression occurring downstream of the royalty measurement point, to the extent the compression is necessary for transportation. This includes compression at the CDP and in the transportation system to the $CO_2$-removal facility. You cannot include those compression costs associated with production operations.

You must convert any payment for transportation that is made in-kind for dehydration and allowable compression to

a dollar equivalent and include this amount in the transportation allowance deduction. You must allocate transportation costs for any allowable dehydration and compression (either in-value or in-kind) between the methane and $CO_2$ in the [s]ame manner as the in-value transportation cost.

You cannot include the costs of removing $CO_2$ as part of your transportation allowance. If you pay a bundled fee for both transportation and $CO_2$ removal and are unable to segregate the fee between these two [s]ervices, the MMS' Valuation and Standards Division will help you determine the proper portion attributable to transportation.

*Processing allowances*

You cannot take a [processing] allowance for your costs of removing $CO_2$.

*Other deductions*

You cannot include any costs associated with moving the production from the wellhead to the CDP (gathering) when the Bureau of Land Management (BLM) has approved the CDP as the royalty measurement point.

You cannot include any costs associated with wellhead separation.

**Reporting Production**

For each lease or agreement producing coalbed methane, you must report the total volume of gas measured at the BLM-approv[e]d royalty measurement point on the Monthly Report of Operations (Form MMS-3160) as a Gas Transfer. Report the four-digit gas plant number and name of the plant receiving the largest volume of gas from the property (if gas is being transferred to more than one plant) in the Plant Number/Name field. If you are using additional plants for $CO_2$ removal, identify the other plant(s) in the Comments section.

Report the Btu content of the gas, as determined at the royalty measurement point, on the API Gravity/Btu Content

line. Report the percentage of $CO_2$ in the gas stream, as measured at the royalty measurement point, in the Comments section.

If you report gas as Used on or for Benefit of Lease, you must be consistent with the approvals of BLM. Do not include any gas used off-lease for compression, dehydration, or $CO_2$ removal unless specifically approved by BLM.

**Reporting Royalty**

For each lease/revenue source combination, you must report the allocated share of the total volume of gas determined at the BLM-approved royalty measurement point in the Sales Quantity field on the Report of Sales and Royalty Remittance (Form MMS-2014). Report the gas as unprocessed gas (Product Code 04) using Transaction Code 01, Royalty Due. Report the Btu content of the gas, as determined at the royalty measurement point, in the Quality Measurement field.

Base the value reported in the Sales Value field on the criteria described in the Valuing Production section of this letter.

Report transportation allowances against Product Code 04 using Transaction Code 11.

If you have any questions about production or royalty reporting, contact the MMS Reports Branch at 800-525-0309 or 303-231-3288.

Sincerely,

/s/ Robert E. Brown

**Robert E. Brown**
**Acting Associate Director for**
**Royalty Management**

## APPENDIX K

## UNITED STATES COURT OF APPEALS
## FOR THE DISTRICT OF COLUMBIA CIRCUIT

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SEPTEMBER TERM, 2004
NO. 04-5006
CONSOLIDATED WITH 04-5007.

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AMOCO PRODUCTION COMPANY,
*APPELLANT*

V.

REBECCA W. WATSON, ASSISTANT SECRETARY FOR LAND AND MINERAL MANAGEMENT, ET AL.,
*APPELLEES*

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00CV01480, 00CV02933
FILED ON: AUGUST 24, 2005

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**Before**: Edwards, Sentelle, and Roberts, Circuit Judges.

**ORDER**

Upon consideration of appellants' petition for rehearing filed July 25, 2005, it is **ORDERED** that the petition be denied.

**Per Curiam**

**FOR THE COURT:**
Mark J. Langer, Clerk

BY:
Michael C. McGrail
Deputy Clerk

## APPENDIX L

## RELEVANT STATUTORY AND REGULATORY PROVISIONS

1. Section 17 of the Mineral Leasing Act of 1920, codified as amended, 30 U.S.C. § 226, 41 Stat. 437, provides, in relevant part:

**§226. Lease of oil and gas lands**

(a) Authority of Secretary

All lands subject to disposition under this chapter which are known or believed to contain oil or gas deposits may be leased by the Secretary.

(b) Lands within known geologic structure of a producing oil or gas field; lands within special tar sand areas; competitive bidding; royalties

(1)(A) All lands to be leased which are not subject to leasing under paragraphs (2) and (3) of this subsection shall be leased as provided in this paragraph to the highest responsible qualified bidder by competitive bidding under general regulations in units of not more than 2,560 acres, except in Alaska, where units shall be not more than 5,760 acres. Such units shall be as nearly compact as possible. Lease sales shall be conducted by oral bidding. Lease sales shall be held for each State where eligible lands are available at least quarterly and more frequently if the Secretary of the Interior determines such sales are necessary. A lease shall be conditioned upon the payment of a royalty at a rate of not less than 12.5 percent in amount or value of the production removed or sold from the lease. The Secretary shall accept the highest bid from a responsible qualified bidder which is equal to or greater than the national minimum acceptable bid, without evaluation of the value of the lands proposed for lease. Leases shall be issued within 60 days following payment by the successful bidder of the remainder of the bonus bid, if any, and the annual rental for the first lease year. All bids for less than

the national minimum acceptable bid shall be rejected. Lands for which no bids are received or for which the highest bid is less than the national minimum acceptable bid shall be offered promptly within 30 days for leasing under subsection (c) of this section and shall remain available for leasing for a period of 2 years after the competitive lease sale.

**(B)** The national minimum acceptable bid shall be $2 per acre for a period of 2 years from December 22, 1987. Thereafter, the Secretary, subject to paragraph (2)(B), may establish by regulation a higher national minimum acceptable bid for all leases based upon a finding that such action is necessary: (i) to enhance financial returns to the United States; and (ii) to promote more efficient management of oil and gas resources on Federal lands. Ninety days before the Secretary makes any change in the national minimum acceptable bid, the Secretary shall notify the Committee on Natural Resources of the United States House of Representatives and the Committee on Energy and Natural Resources of the United States Senate. The proposal or promulgation of any regulation to establish a national minimum acceptable bid shall not be considered a major Federal action subject to the requirements of section 4332(2)(C) of Title 42.

**(2)(A)(i)** If the lands to be leased are within a special tar sand area, they shall be leased to the highest responsible qualified bidder by competitive bidding under general regulations in units of not more than 5,760 acres, which shall be as nearly compact as possible, upon the payment by the lessee of such bonus as may be accepted by the Secretary.

**(ii)** Royalty shall be 12 1/2 per centum in amount or value of production removed or sold from the lease, subject to subsection (k)(1)(c) of this section.

**(iii)** The Secretary may lease such additional lands in special tar sand areas as may be required in support

of any operations necessary for the recovery of tar sands.

**(iv)** No lease issued under this paragraph shall be included in any chargeability limitation associated with oil and gas leases.

**(B)** For any area that contains any combination of tar sand and oil or gas (or both), the Secretary may issue under this chapter, separately—

**(i)** a lease for exploration for and extraction of tar sand; and

**(ii)** a lease for exploration for and development of oil and gas.

**(C)** A lease issued for tar sand shall be issued using the same bidding process, annual rental, and posting period as a lease issued for oil and gas, except that the minimum acceptable bid required for a lease issued for tar sand shall be $2 per acre.

2. Section 2 of the Act of July 18, 1966, codified as amended at 28 U.S.C. § 2415, 80 Stat. 304, provides, in relevant part:

**§ 2415. Time for commencing actions brought by the United States**

**(a)** Subject to the provisions of section 2416 of this title, and except as otherwise provided by Congress, every action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later: *Provided*, That in the event of later partial payment or written acknowledgment of debt, the right of action shall be deemed to accrue again at the time of each such payment or acknowledgment: *Provided further*, That an action for money damages brought by the United States for or on behalf of a recognized tribe, band or group of American Indians shall not be barred unless the complaint is filed more than six years and ninety days after the right of action accrued: *Provided further*, That an action for money damages which accrued on the date of enactment of this Act in accordance with subsection (g) brought by the United States for or on behalf of a recognized tribe, band, or group of American Indians, or on behalf of an individual Indian whose land is held in trust or restricted status, shall not be barred unless the complaint is filed sixty days after the date of publication of the list required by section 4(c) of the Indian Claims Limitation Act of 1982: *Provided*, That, for those claims that are on either of the two lists published pursuant to the Indian Claims Limitation Act of 1982, any right of action shall be barred unless the complaint is filed within (1) one year after the Secretary of the Interior has published in the Federal Register a notice rejecting such

claim or (2) three years after the date the Secretary of the Interior has submitted legislation or legislative report to Congress to resolve such claim or more than two years after a final decision has been rendered in applicable administrative proceedings required by contract or by law, whichever is later.

**(b)** Subject to the provisions of section 2416 of this title, and except as otherwise provided by Congress, every action for money damages brought by the United States or an officer or agency thereof which is founded upon a tort shall be barred unless the complaint is filed within three years after the right of action first accrues: *Provided*, That an action to recover damages resulting from a trespass on lands of the United States; an action to recover damages resulting from fire to such lands; an action to recover for diversion of money paid under a grant program; and an action for conversion of property of the United States may be brought within six years after the right of action accrues, except that such actions for or on behalf of a recognized tribe, band or group of American Indians, including actions relating to allotted trust or restricted Indian lands, may be brought within six years and ninety days after the right of action accrues, except that such actions for or on behalf of a recognized tribe, band, or group of American Indians, including actions relating to allotted trust or restricted Indian lands, or on behalf of an individual Indian whose land is held in trust or restricted status which accrued on the date of enactment of this Act in accordance with subsection (g) may be brought on or before sixty days after the date of the publication of the list required by section 4(c) of the Indian Claims Limitation Act of 1982: *Provided*, That, for those claims that are on either of the two lists published pursuant to the Indian Claims Limitation Act of 1982, any right of action shall be barred unless the complaint is filed within (1) one year after the Secretary of the Interior has published in the Federal Register a notice rejecting such claim or (2)

three years after the Secretary of the Interior has submitted legislation or legislative report to Congress to resolve such claim.

(c) Nothing herein shall be deemed to limit the time for bringing an action to establish the title to, or right of possession of, real or personal property.

(d) Subject to the provisions of section 2416 of this title and except as otherwise provided by Congress, every action for the recovery of money erroneously paid to or on behalf of any civilian employee of any agency of the United States or to or on behalf of any member or dependent of any member of the uniformed services of the United States, incident to the employment or services of such employee or member, shall be barred unless the complaint is filed within six years after the right of action accrues: *Provided*, That in the event of later partial payment or written acknowledgment of debt, the right of action shall be deemed to accrue again at the time of each such payment or acknowledgment.

(e) In the event that any action to which this section applies is timely brought and is thereafter dismissed without prejudice, the action may be recommenced within one year after such dismissal, regardless of whether the action would otherwise then be barred by this section. In any action so recommenced the defendant shall not be barred from interposing any claim which would not have been barred in the original action.

(f) The provisions of this section shall not prevent the assertion, in an action against the United States or an officer or agency thereof, of any claim of the United States or an officer or agency thereof against an opposing party, a co-party, or a third party that arises out of the transaction or occurrence that is the subject matter of the opposing party's claim. A claim of the United States or an officer or agency thereof that does not arise out of the transaction or

occurrence that is the subject matter of the opposing party's claim may, if time-barred, be asserted only by way of offset any may be allowed in an amount not to exceed the amount of the opposing party's recovery.

(g) Any right of action subject to the provisions of this section which accrued prior to the date of enactment of this Act shall, for purposes of this section, be deemed to have accrued on the date of enactment of this Act.

(h) Nothing in this Act shall apply to actions brought under the Internal Revenue Code or incidental to the collection of taxes imposed by the United States.

(i) The provisions of this section shall not prevent the United States or an officer or agency thereof from collecting any claim of the United States by means of administrative offset, in accordance with section 3716 of title 31.

3. Section 206 of Title 30 of the Code of Federal Regulations provides, in relevant part:

**§ 206.151 Definitions.**

For purposes of this subpart:

"*Allowance*" means an approved or an MMS-initially accepted deduction in determining value for royalty purposes. "Processing allowance" means an allowance for the reasonable, actual costs incurred by the lessee for processing gas, or an approved or MMS-initially accepted deduction for costs of such processing, determined pursuant to this subpart. "Transportation allowance" means an allowance for the reasonable, actual costs incurred by the lessee for moving unprocessed gas, residue gas, or gas plant products to a point of sale or point of delivery off the lease, unit area, communitized area, or away from a processing plant, excluding gathering, or an approved or MMS-initially accepted deduction for costs of such transportation, determined pursuant to this subpart.

"*Area*" means a geographic region at least as large as the defined limits of an oil and/or gas field, in which oil and/or gas lease products have similar quality, economic, and legal characteristics.

"*Arm's length contract*" means a contract or agreement that has been arrived at in the marketplace between independent, nonaffiliated persons with opposing economic interests regarding that contract. For purposes of this subpart, two persons are affiliated if one person controls, is controlled by, or is under common control with another person. For purposes of this subpart, based on the instruments of ownership of the voting securities of an entity, or based on other forms of ownership:

(a) Ownership in excess of 50 percent constitutes control;

(b) Ownership of 10 through 50 percent creates a presumption of control; and

(c) Ownership of less than 10 percent creates a presumption of noncontrol which MMS may rebut if it demonstrates actual or legal control, including the existence of interlocking directorates.

Notwithstanding any other provisions of this subpart, contracts between relatives, either by blood or by marriage, are not arm's-length contracts. The MMS may require the lessee to certify ownership control. To be considered arm's-length for any production month, a contract must meet the requirements of this definition for that production month as well as when the contract was executed.

*"Audit"* means a review, conducted in accordance with generally accepted accounting and auditing standards, of royalty payment compliance activities of lessees or other interest holders who pay royalties, rents, or bonuses on Federal and Indian leases.

*"BIA"* means the Bureau of Indian Affairs of the Department of the Interior.

*"BLM"* means the Bureau of Land Management of the Department of the Interior.

*"Compression"* means the process of raising the pressure of gas.

*"Condensate"* means liquid hydrocarbons (normally exceeding 40 degrees of API gravity) recovered at the surface without resorting to processing. Condensate is the mixture of liquid hydrocarbons that results from condensation of petroleum hydrocarbons existing initially in a gaseous phase in an underground reservoir.

*"Contract"* means any oral or written agreement, including amendments or revisions thereto, between two or more persons and enforceable by law that with due consideration creates an obligation.

*"Field"* means a geographic region situated over one or more subsurface oil and gas reservoirs encompassing at least the outermost boundaries of all oil and gas accumu-

lations known to be within those reservoirs vertically projected to the land surface. Onshore fields are usually given names and their official boundaries are often designated by oil and gas regulatory agencies in the respective States in which the fields are located. Outer Continental Shelf (OCS) fields are named and their boundaries are designated by MMS.

*"Gas"* means any fluid, either combustible or noncombustible, hydrocarbon or nonhydrocarbon, which is extracted from a reservoir and which has neither independent shape nor volume, but tends to expand indefinitely. It is a substance that exists in a gaseous or rarefied state under standard temperature and pressure conditions.

*"Gas plant products"* means separate marketable elements, compounds, or mixtures, whether in liquid, gaseous, or solid form, resulting from processing gas, excluding residue gas.

*"Gathering"* means the movement of lease production to a central accumulation and/or treatment point on the lease, unit or communitized area, or to a central accumulation or treatment point off the lease, unit or communitized area as approved by BLM or MMS OCS operations personnel for onshore and OCS leases, respectively.

*"Gross proceeds"* (for royalty payment purposes) means the total monies and other consideration accruing to an oil and gas lessee for the disposition of unprocessed gas, residue gas, or gas plant products. Gross proceeds includes, but is not limited to, payments to the lessee for certain services such as compression, dehydration, measurement, and/or field gathering to the extent that the lessee is obligated to perform them at no cost to the Federal Government or Indian lessor, and payments for gas processing rights. Gross proceeds, as applied to gas, also includes but is not limited to: Take-or-pay payments; reimbursements for severance taxes; and other reimbursements. Tax reim-

bursements are part of the gross proceeds accruing to a lessee even though the Federal or Indian royalty interest may be exempt from taxation. Payments or credits for advanced exploration or development costs or prepaid reserve payments that are subject to recoupment through credits against the purchase price or through reduced prices in later sales and which are made before production commences become part of gross proceeds as of the time of first production. Monies and other consideration, including the forms of consideration identified in this paragraph, to which a lessee is contractually or legally entitled but which it does not seek to collect through reasonable efforts are also part of gross proceeds.

*"Indian allottee"* means any Indian for whom land or an interest in land is held in trust by the United States or who holds title subject to Federal restriction against alienation.

*"Indian Tribe"* means any Indian Tribe, band, nation, pueblo, community, rancheria, colony, or other group of Indians for which any land or interest in land is held in trust by the United States or which is subject to Federal restriction against alienation.

*"Lease"* means any contract, profit-share arrangement, joint venture, or other agreement issued or approved by the United States under a mineral leasing law that authorizes exploration for, development or extraction of, or removal of lease products—or the land area covered by that authorization, whichever is required by the context.

*"Lease products"* means any leased minerals attributable to, originating from, or allocated to Outer Continental Shelf or onshore Federal or Indian leases.

*"Lessee"* means any person to whom the United States, an Indian Tribe, or an Indian allottee issues a lease, and any person who has been assigned an obligation to make royalty or other payments required by the lease. This includes any person who has an interest in a lease as well as an operator

or payor who has no interest in the lease but who has assumed the royalty payment responsibility.

*"Like-quality lease products"* means lease products which have similar chemical, physical, and legal characteristics.

*"Marketable condition"* means lease products which are sufficiently free from impurities and otherwise in a condition that they will be accepted by a purchaser under a sales contract typical for the field or area.

*"Marketing affiliate"* means an affiliate of the lessee whose function is to acquire only the lessee's production and to market that production.

*"Minimum royalty"* means that minimum amount of annual royalty that the lessee must pay as specified in the lease or in applicable leasing regulations.

*"Net-back method"* (or work-back method) means a method for calculating market value of gas at the lease. Under this method, costs of transportation, processing, or manufacturing are deducted from the proceeds received for the gas, residue gas or gas plant products, and any extracted, processed, or manufactured products, or from the value of the gas, residue gas or gas plant products, and any extracted, processed, or manufactured products, at the first point at which reasonable values for any such products may be determined by a sale pursuant to an arm's-length contract or comparison to other sales of such products, to ascertain value at the lease.

*"Net output"* means the quantity of residue gas and each gas plant product that a processing plant produces.

*"Net profit share"* (for applicable Federal and Indian leases) means the specified share of the net profit from production of oil and gas as provided in the agreement.

*"Outer Continental Shelf (OCS)"* means all submerged lands lying seaward and outside of the area of land beneath navigable waters as defined in section 2 of the Submerged

Lands Act (43 U.S.C. 1301) and of which the subsoil and seabed appertain to the United States and are subject to its jurisdiction and control.

*"Person"* means any individual, firm, corporation, association, partnership, consortium, or joint venture (when established as a separate entity).

*"Posted price"* means the price, net of all adjustments for quality and location, specified in publicly available price bulletins or other price notices available as part of normal business operations for quantities of unprocessed gas, residue gas, or gas plant products in marketable condition.

*"Processing"* means any process designed to remove elements or compounds (hydrocarbon and nonhydrocarbon) from gas, including absorption, adsorption, or refrigeration. Field processes which normally take place on or near the lease, such as natural pressure reduction, mechanical separation, heating, cooling, dehydration, and compression, are not considered processing. The changing of pressures and/or temperatures in a reservoir is not considered processing.

*"Residue gas"* means that hydrocarbon gas consisting principally of methane resulting from processing gas.

*"Section 6 lease"* means an OCS lease subject to section 6 of the Outer Continental Shelf Lands Act, as amended, 43 U.S.C. 1335.

*"Selling arrangement"* means the individual contractual arrangements under which sales or dispositions of gas, residue gas and gas plant products are made. Selling arrangements are described by illustration in the MMS Royalty Management Program Oil and Gas Payor Handbook.

*"Spot sales agreement"* means a contract wherein a seller agrees to sell to a buyer a specified amount of unprocessed gas, residue gas, or gas plant products at a specified price over a fixed period, usually of short duration, which does not normally require a cancellation notice to ter-

minate, and which does not contain an obligation, nor imply an intent, to continue in subsequent periods.

*"Warranty contract"* means a long-term contract entered into prior to 1970, including any amendments thereto, for the sale of gas wherein the producer agrees to sell a specific amount of gas and the gas delivered in satisfaction of this obligation may come from fields or sources outside of the designated fields.

**§ 206.152 Valuation standards–unprocessed gas.**

(a)(1) This section applies to the valuation of all gas that is not processed and all gas that is processed but is sold or otherwise disposed of by the lessee pursuant to an arm's-length contract prior to processing. Where the lessee's contract includes a reservation of the right to process the gas and the lessee exercises that right, or where the lessee's contract for the sale of gas prior to processing provides for the value to be determined based upon a percentage of the purchaser's proceeds resulting from processing the gas, § 206.153 shall apply instead of this section. This section also applies to processed gas which must be valued prior to processing in accordance with § 206.155.

(2) The value of production, for royalty purposes, of gas subject to this subpart shall be the value of gas determined pursuant to this section less applicable allowances determined pursuant to this subpart.

(3)(i) For any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value of production for royalty purposes, if data are available to compute a major portion MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production for royalty purposes shall be the higher of those two values.

(ii) For purposes of this paragraph, major portion means the highest price paid or offered at the time of production for the major portion of gas production from the same field. The major portion will be calculated using like-quality gas sold under arm's-length contracts from the same field (or, if necessary to obtain a reasonable sample, from the same area) for each month. All such sales will be arrayed from highest price to lowest price (at the bottom). The major portion is that price at which 50 percent (by volume) plus 1 mcf of the gas (starting from the bottom) is sold.

(b)(1)(i) The value of gas which is sold pursuant to an arm's-length contract shall be the gross proceeds accruing to the lessee, except as provided in paragraphs (b)(1) (ii) and (iii) of this section. The lessee shall have the burden of demonstrating that its contract is arm's-length. The value which the lessee reports, for royalty purposes, is subject to monitoring, review, and audit. For purposes of this section, gas which is sold or otherwise transferred to the lessee's marketing affiliate and then sold by the marketing affiliate pursuant to an arm's-length contract shall be valued in accordance with this paragraph based upon the sale by the marketing affiliate.

(ii) In conducting reviews and audits, MMS will examine whether the contract reflects the total consideration actually transferred either directly or indirectly from the buyer to the seller for the gas. If the contract does not reflect the total consideration, then the MMS may require that the gas sold pursuant to that contract be valued in accordance with paragraph (c) of this section. Value may not be less than the gross proceeds accruing to the lessee, including the additional consideration.

(iii) If the MMS determines that the gross proceeds accruing to the lessee pursuant to an arm's-length contract do not reflect the reasonable value of the production because of misconduct by or between the contracting parties, or because the lessee otherwise has breached its duty to the

lessor to market the production for the mutual benefit of the lessee and the lessor, then MMS shall require that the gas production be valued pursuant to paragraphs (c)(2) or (c)(3) of this section, and in accordance with the notification requirements of paragraph (e) of this section. When MMS determines that the value may be unreasonable, MMS will notify the lessee and give the lessee an opportunity to provide written information justifying the lessee's value.

(2) Notwithstanding the provisions of paragraph (b)(1) of this section, the value of gas sold pursuant to a warranty contract shall be determined by MMS, and due consideration will be given to all valuation criteria specified in this section. The lessee must request a value determination in accordance with paragraph (g) of this section for gas sold pursuant to a warranty contract; provided, however, that any value determination for a warranty contract in effect on the effective date of these regulations shall remain in effect until modified by MMS.

(3) MMS may require a lessee to certify that its arm's-length contract provisions include all of the consideration to be paid by the buyer, either directly or indirectly, for the gas.

(c) The value of gas subject to this section which is not sold pursuant to an arm's-length contract shall be the reasonable value determined in accordance with the first applicable of the following methods:

(1) The gross proceeds accruing to the lessee pursuant to a sale under its non-arm's-length contract (or other disposition other than by an arm's-length contract), provided that those gross proceeds are equivalent to the gross proceeds derived from, or paid under, comparable arm's-length contracts for purchases, sales, or other dispositions of like-quality gas in the same field (or, if necessary to obtain a reasonable sample, from the same area). In evaluating the comparability of arm's-length con-

tracts for the purposes of these regulations, the following factors shall be considered: price, time of execution, duration, market or markets served, terms, quality of gas, volume, and such other factors as may be appropriate to reflect the value of the gas;

(2) A value determined by consideration of other information relevant in valuing like-quality gas, including gross proceeds under arm's-length contracts for like-quality gas in the same field or nearby fields or areas, posted prices for gas, prices received in arm's-length spot sales of gas, other reliable public sources of price or market information, and other information as to the particular lease operation or the saleability of the gas; or

(3) A net-back method or any other reasonable method to determine value.

(d)(1) Notwithstanding any other provisions of this section, except paragraph (h) of this section, if the maximum price permitted by Federal law at which gas may be sold is less than the value determined pursuant to this section, then MMS shall accept such maximum price as the value. For purposes of this section, price limitations set by any State or local government shall not be considered as a maximum price permitted by Federal law.

(2) The limitation prescribed in paragraph (d)(1) of this section shall not apply to gas sold pursuant to a warranty contract and valued pursuant to paragraph (b)(2) of this section.

(e)(1) Where the value is determined pursuant to paragraph (c) of this section, the lessee shall retain all data relevant to the determination of royalty value. Such data shall be subject to review and audit, and MMS will direct a lessee to use a different value if it determines that the reported value is inconsistent with the requirements of these regulations.

(2) Any Federal or Indian lessee will make available upon request to the authorized MMS, State, or Indian representatives, to the Office of the Inspector General of the Department of the Interior, or other person authorized to receive such information, arm's-length sales and volume data for like-quality production sold, purchased or otherwise obtained by the lessee from the field or area or from nearby fields or areas.

(3) A lessee shall notify MMS if it has determined value pursuant to paragraph (c)(2) or (c)(3) of this section. The notification shall be by letter to the MMS Associate Director for Royalty Management or his/her designee. The letter shall identify the valuation method to be used and contain a brief description of the procedure to be followed. The notification required by this paragraph is a one-time notification due no later than the end of the month following the month the lessee first reports royalties on a Form MMS-2014 using a valuation method authorized by paragraph (c)(2) or (c)(3) of this section, and each time there is a change in a method under paragraph (c)(2) or (c)(3) of this section.

(f) If MMS determines that a lessee has not properly determined value, the lessee shall pay the difference, if any, between royalty payments made based upon the value it has used and the royalty payments that are due based upon the value established by MMS. The lessee shall also pay interest on that difference computed pursuant to 30 C.F.R. 218.54. If the lessee is entitled to a credit, MMS will provide instructions for the taking of that credit.

(g) The lessee may request a value determination from MMS. In that event, the lessee shall propose to MMS a value determination method, and may use that method in determining value for royalty purposes until MMS issues its decision. The lessee shall submit all available data relevant to its proposal. The MMS shall expeditiously determine the value based upon the lessee's proposal and any additional

information MMS deems necessary. In making a value determination MMS may use any of the valuation criteria authorized by this subpart. That determination shall remain effective for the period stated therein. After MMS issues its determination, the lessee shall make the adjustments in accordance with paragraph (f) of this section.

(h) Notwithstanding any other provision of this section, under no circumstances shall the value of production for royalty purposes be less than the gross proceeds accruing to the lessee for lease production, less applicable allowances determined pursuant to this subpart.

(i) The lessee is required to place gas in marketable condition at no cost to the Federal Government or Indian lessor unless otherwise provided in the lease agreement. Where the value established pursuant to this section is determined by a lessee's gross proceeds, that value shall be increased to the extent that the gross proceeds have been reduced because the purchaser, or any other person, is providing certain services the cost of which ordinarily is the responsibility of the lessee to place the gas in marketable condition.

(j) Value shall be based on the highest price a prudent lessee can receive through legally enforceable claims under its contract. If there is no contract revision or amendment, and the lessee fails to take proper or timely action to receive prices or benefits to which it is entitled, it must pay royalty at a value based upon that obtainable price or benefit. Contract revisions or amendments shall be in writing and signed by all parties to an arm's-length contract. If the lessee makes timely application for a price increase or benefit allowed under its contract but the purchaser refuses, and the lessee takes reasonable measures, which are documented, to force purchaser compliance, the lessee will owe no additional royalties unless or until monies or consideration resulting from the price increase or additional benefits are received. This paragraph shall not be con-

strued to permit a lessee to avoid its royalty payment obligation in situations where a purchaser fails to pay, in whole or in part or timely, for a quantity of gas.

(k) Notwithstanding any provision in these regulations to the contrary, no review, reconciliation, monitoring, or other like process that results in a redetermination by the MMS of value under this section shall be considered final or binding as against the Federal Government, its beneficiaries, the Indian Tribes, or allottees until the audit period is formally closed.

(l) Certain information submitted to MMS to support valuation proposals, including transportation or extraordinary cost allowances, is exempted from disclosure by the Freedom of Information Act, 5 U.S.C. 552, or other Federal Law. Any data specified by law to be privileged, confidential, or otherwise exempt will be maintained in a confidential manner in accordance with applicable law and regulations. All requests for information about determinations made under this subpart are to be submitted in accordance with the Freedom of Information Act regulation of the Department of the Interior, 43 C.F.R. Part 2. Nothing in this section is intended to limit or diminish in any manner whatsoever the right of an Indian lessor to obtain any and all information as such lessor may be lawfully entitled from MMS or such lessor's lessee directly under the terms of the lease, 30 U.S.C. 1733, or other applicable law.

**§ 206.153 Valuation standards–processed gas.**

(a)(1) This section applies to the valuation of all gas that is processed by the lessee and any other gas production to which this subpart applies and that is not subject to the valuation provisions of § 206.152 of this subpart. This section applies where the lessee's contract includes a reservation of the right to process the gas and the lessee exercises that right, or where the lessee's contract for the sale of gas prior to processing provides for the value to be deter-

mined based upon a percentage of the purchaser's proceeds resulting from processing the gas (in which event these regulations will apply to determine value as if the person actually selling or disposing of the residue gas or gas plant products were the lessee of the Federal or Indian lease).

(2) The value of production, for royalty purposes, of gas subject to this section shall be the combined value of the residue gas and all gas plant products determined pursuant to this section, plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing determined pursuant to § 206.102 of this part, less applicable transportation allowances and processing allowances determined pursuant to this subpart.

(3)(i) For any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value for royalty purposes, if data are available to compute a major portion MMS will, where practicable, compare the values determined in accordance with this section for any lease product with the major portion determined for that lease product. The value to be used in determining the value of production for royalty purposes shall be the higher of those two values.

(ii) For purposes of this paragraph, major portion means the highest price paid or offered at the time of production for the major portion of gas production from the same field, or for residue gas or gas plant products from the same processing plant, as applicable. The major portion will be calculated using like-quality lease products sold under arm's-length contracts from the same field or processing plant (or, if necessary to obtain a reasonable sample, from the same area or nearby processing plants) for each month. All such sales will be arrayed from highest price to lowest price (at the bottom). The major portion is that price at which 50 percent (by volume) plus 1 mcf of the gas (starting

from the bottom) is sold, or for gas plant products, 50 percent (by volume) plus 1 unit.

(b)(1)(i) The value of the residue gas or any gas plant product which is sold pursuant to an arm's-length contract shall be the gross proceeds accruing to the lessee, except as provided in paragraphs (b)(1) (ii) and (iii) of this section. The lessee shall have the burden of demonstrating that its contract is arm's-length. The value that the lessee reports for royalty purposes is subject to monitoring, review, and audit. For purposes of this section, residue gas or any gas plant product which is sold or otherwise transferred to the lessee's marketing affiliate and then sold by the marketing affiliate pursuant to an arm's-length contract shall be valued in accordance with this paragraph based upon the sale by the marketing affiliate.

(ii) In conducting these reviews and audits, MMS will examine whether or not the contract reflects the total consideration actually transferred either directly or indirectly from the buyer to the seller for the residue gas or gas plant product. If the contract does not reflect the total consideration, then the MMS may require that the residue gas or gas plant product sold pursuant to that contract be valued in accordance with paragraph (c) of this section. Value may not be less than the gross proceeds accruing to the lessee, including the additional consideration.

(iii) If the MMS determines that the gross proceeds accruing to the lessee pursuant to an arm's-length contract do not reflect the reasonable value of the residue gas or gas plant product because of misconduct by or between the contracting parties, or because the lessee otherwise has breached its duty to the lessor to market the production for the mutual benefit of the lessee and the lessor, then MMS shall require that the residue gas or gas plant product be valued pursuant to paragraphs (c)(2) or (c)(3) of this section, and in accordance with the notification requirements of paragraph (e) of this section. When MMS determines that

the value may be unreasonable, MMS will notify the lessee and give the lessee an opportunity to provide written information justifying the lessee's value.

(2) Notwithstanding the provisions of paragraph (b)(1) of this section, the value of residue gas sold pursuant to a warranty contract shall be determined by MMS, and due consideration will be given to all valuation criteria specified in this section. The lessee must request a value determination in accordance with paragraph (g) of this section for gas sold pursuant to a warranty contract; provided, however, that any value determination for a warranty contract in effect on the effective date of these regulations shall remain in effect until modified by MMS.

(3) MMS may require a lessee to certify that its arm's-length contract provisions include all of the consideration to be paid by the buyer, either directly or indirectly, for the residue gas or gas plant product.

(c) The value of residue gas or any gas plant product which is not sold pursuant to an arm's-length contract shall be the reasonable value determined in accordance with the first applicable of the following methods:

(1) The gross proceeds accruing to the lessee pursuant to a sale under its non-arm's-length contract (or other disposition other than by an arm's-length contract), provided that those gross proceeds are equivalent to the gross proceeds derived from, or paid under, comparable arm's-length contracts for purchases, sales, or other dispositions of like quality residue gas or gas plant products from the same processing plant (or, if necessary to obtain a reasonable sample, from nearby plants). In evaluating the comparability of arm's-length contracts for the purposes of these regulations, the following factors shall be considered: price, time of execution, duration, market or markets served, terms, quality of residue gas or gas plant products, volume,

and such other factors as may be appropriate to reflect the value of the residue gas or gas plant products;

(2) A value determined by consideration of other information relevant in valuing like-quality residue gas or gas plant products, including gross proceeds under arm's-length contracts for like-quality residue gas or gas plant products from the same gas plant or other nearby processing plants, posted prices for residue gas or gas plant products, prices received in spot sales of residue gas or gas plant products, other reliable public sources of price or market information, and other information as to the particular lease operation or the saleability of such residue gas or gas plant products; or

(3) A net-back method or any other reasonable method to determine value.

(d)(1) Notwithstanding any other provisions of this section, except paragraph (h) of this section, if the maximum price permitted by Federal law at which any residue gas or gas plant products may be sold is less than the value determined pursuant to this section, then MMS shall accept such maximum price as the value. For the purposes of this section, price limitations set by any State or local government shall not be considered as a maximum price permitted by Federal law.

(2) The limitation prescribed by paragraph (d)(1) of this section shall not apply to residue gas sold pursuant to a warranty contract and valued pursuant to paragraph (b)(2) of this section.

(e)(1) Where the value is determined pursuant to paragraph (c) of this section, the lessee shall retain all data relevant to the determination of royalty value. Such data shall be subject to review and audit, and MMS will direct a lessee to use a different value if it determines upon review or audit that the reported value is inconsistent with the requirements of these regulations.

(2) Any Federal or Indian lessee will make available upon request to the authorized MMS, State, or Indian representatives, to the Office of the Inspector General of the Department of the Interior, or other persons authorized to receive such information, arm's-length sales and volume data for like-quality residue gas and gas plant products sold, purchased or otherwise obtained by the lessee from the same processing plant or from nearby processing plants.

(3) A lessee shall notify MMS if it has determined any value pursuant to paragraph (c)(2) or (c)(3) of this section. The notification shall be by letter to the MMS Associate Director for Royalty Management or his/her designee. The letter shall identify the valuation method to be used and contain a brief description of the procedure to be followed. The notification required by this paragraph is a one-time notification due no later than the end of the month following the month the lessee first reports royalties on a Form MMS-2014 using a valuation method authorized by paragraph (c)(2) or (c)(3) of this section, and each time there is a change in a method under paragraph (c)(2) or (c)(3) of this section.

(f) If MMS determines that a lessee has not properly determined value, the lessee shall pay the difference, if any, between royalty payments made based upon the value it has used and the royalty payments that are due based upon the value established by MMS. The lessee shall also pay interest computed on that difference pursuant to 30 C.F.R. 218.54. If the lessee is entitled to a credit, MMS will provide instructions for the taking of that credit.

(g) The lessee may request a value determination from MMS. In that event, the lessee shall propose to MMS a value determination method, and may use that method in determining value for royalty purposes until MMS issues its decision. The lessee shall submit all available data relevant to its proposal. The MMS shall expeditiously determine the value based upon the lessee's proposal and any additional

information MMS deems necessary. In making a value determination, MMS may use any of the valuation criteria authorized by this subpart. That determination shall remain effective for the period stated therein. After MMS issues its determination, the lessee shall make the adjustments in accordance with paragraph (f) of this section.

(h) Notwithstanding any other provision of this section, under no circumstances shall the value of production for royalty purposes be less than the gross proceeds accruing to the lessee for residue gas and/or any gas plant products, less applicable transportation allowances and processing allowances determined pursuant to this subpart.

(i) The lessee is required to place residue gas and gas plant products in marketable condition at no cost to the Federal Government or Indian lessor unless otherwise provided in the lease agreement. Where the value established pursuant to this section is determined by a lessee's gross proceeds, that value shall be increased to the extent that the gross proceeds have been reduced because the purchaser, or any other person, is providing certain services the cost of which ordinarily is the responsibility of the lessee to place the residue gas or gas plant products in marketable condition.

(j) Value shall be based on the highest price a prudent lessee can receive through legally enforceable claims under its contract. Absent contract revision or amendment, if the lessee fails to take proper or timely action to receive prices or benefits to which it is entitled it must pay royalty at a value based upon that obtainable price or benefit. Contract revisions or amendments shall be in writing and signed by all parties to an arm's-length contract. If the lessee makes timely application for a price increase or benefit allowed under its contract but the purchaser refuses, and the lessee takes reasonable measures, which are documented, to force purchaser compliance, the lessee will owe no additional royalties unless or until monies or consideration resulting

from the price increase or additional benefits are received. This paragraph shall not be construed to permit a lessee to avoid its royalty payment obligation in situations where a purchaser fails to pay, in whole or in part, or timely, for a quantity of residue gas or gas plant product.

(k) Notwithstanding any provision in these regulations to the contrary, no review, reconciliation, monitoring, or other like process that results in a redetermination by MMS of value under this section shall be considered final or binding against the Federal Government, its beneficiaries, the Indian Tribes, or allottees, until the audit period is formally closed.

(l) Certain information submitted to MMS to support valuation proposals, including transportation allowances, processing allowances or extraordinary cost allowances, is exempted from disclosure by the Freedom of Information Act, 5 U.S.C. 552, or other Federal law. Any data specified by law to be privileged, confidential, or otherwise exempt, will be maintained in a confidential manner in accordance with applicable law and regulations. All requests for information about determinations made under this Part are to be submitted in accordance with the Freedom of Information Act regulation of the Department of the Interior, 43 C.F.R. Part 2. Nothing in this section is intended to limit or diminish in any manner whatsoever the right of an Indian lessor to obtain any and all information as such lessor may be lawfully entitled from the MMS or such lessor's lessee directly under the terms of the lease, 30 U.S.C. 1733, or other applicable law.

**§ 206.154 Determination of quantities and qualities for computing royalties.**

(a)(1) Royalties shall be computed on the basis of the quantity and quality of unprocessed gas at the point of royalty settlement approved by BLM or MMS for onshore and OCS leases, respectively.

(2) If the value of gas determined pursuant to § 206.152 of this subpart is based upon a quantity and/or quality that is different from the quantity and/or quality at the point of royalty settlement, as approved by BLM or MMS, that value shall be adjusted for the differences in quantity and/or quality.

(b)(1) For residue gas and gas plant products, the quantity basis for computing royalties due is the monthly net output of the plant even though residue gas and/or gas plant products may be in temporary storage.

(2) If the value of residue gas and/or gas plant products determined pursuant to § 206.153 of this subpart is based upon a quantity and/or quality of residue gas and/or gas plant products that is different from that which is attributable to a lease, determined in accordance with paragraph (c) of this section, that value shall be adjusted for the differences i quantity and/or quality.

(c) The quantity of the residue gas and gas plant products attributable to a lease shall be determined according to the following procedure:

(1) When the net output of the processing plant is derived from gas obtained from only one lease, the quantity of the residue gas and gas plant products on which computations of royalty are based is the net output of the plant.

(2) When the net output of a processing plant is derived from gas obtained from more than one lease producing gas of uniform content, the quantity of the residue gas and gas plant products allocable to each lease shall be in the same proportions as the ratios obtained by dividing the amount of gas delivered to the plant from each lease by the total amount of gas delivered from all leases.

(3) When the net output of a processing plant is derived from gas obtained from more than one lease producing gas of nonuniform content, the quantity of the residue gas allocable to each lease will be determined by multiplying the

amount of gas delivered to the plant from the lease by the residue gas content of the gas, and dividing the arithmetical product thus obtained by the sum of the similar arithmetical products separately obtained for all leases from which gas is delivered to the plant, and then multiplying the net output of the residue gas by the arithmetic quotient obtained. The net output of gas plant products allocable to each lease will be determined by multiplying the amount of gas delivered to the plant from the lease by the gas plant product content of the gas, and dividing the arithmetical product thus obtained by the sum of the similar arithmetical products separately obtained for all leases from which gas is delivered to the plant, and then multiplying the net output of each gas plant product by the arithmetic quotient obtained.

(4) A lessee may request MMS approval of other methods for determining the quantity of residue gas and gas plant products allocable to each lease. If approved, such method will be applicable to all gas production from Federal and Indian leases that is processed in the same plant.

(d)(1) No deductions may be made from the royalty volume or royalty value for actual or theoretical losses. Any actual loss of unprocessed gas that may be sustained prior to the royalty settlement metering or measurement point will not be subject to royalty provided that such loss is determined to have been unavoidable by BLM or MMS, as appropriate.

(2) Except as provided in paragraph (d)(1) of this section and 30 C.F.R. 202.151(c), royalties are due on 100 percent of the volume determined in accordance with paragraphs (a) through (c) of this section. There can be no reduction in that determined volume for actual losses after the quantity basis has been determined or for theoretical losses that are claimed to have taken place. Royalties are due on 100 percent of the value of the unprocessed gas, residue gas, and/or

gas plant products as provided in this subpart, less applicable allowances. There can be no deduction from the value of the unprocessed gas, residue gas, and/or gas plant products to compensate for actual losses after the quantity basis has been determined, or for theoretical losses that are claimed to have taken place.

**§ 206.155 Accounting for comparison.**

(a) Except as provided in paragraph (b) of this section, where the lessee (or a person to whom the lessee has transferred gas pursuant to a non-arm's-length contract or without a contract) processes the lessee's gas and after processing the gas the residue gas is not sold pursuant to an arm's-length contract, the value, for royalty purposes, shall be the greater of (1) the combined value, for royalty purposes, of the residue gas and gas plant products resulting from processing the gas determined pursuant to § 206.153 of this subpart, plus the value, for royalty purposes, of any condensate recovered downstream of the point of royalty settlement without resorting to processing determined pursuant to § 206.102 of this subpart; or (2) the value, for royalty purposes, of the gas prior to processing determined in accordance with § 206.152 of this subpart.

(b) The requirement for accounting for comparison contained in the terms of leases, particularly Indian leases, will govern as provided in § 206.150(b) of this subpart. When accounting for comparison is required by the lease terms, such accounting for comparison shall be determined in accordance with paragraph (a) of this section.

**§ 206.156 Transportation allowances–general.**

(a) Where the value of gas has been determined pursuant to § 206.152 or § 206.153 of this subpart at a point (e.g., sales point or point of value determination) off the lease, MMS shall allow a deduction for the reasonable actual costs incurred by the lessee to transport unprocessed gas, residue gas, and gas plant products from a lease to a

point off the lease including, if appropriate, transportation from the lease to a gas processing plant off the lease and from the plant to a point away from the plant.

(b) Transportation costs must be allocated among all products produced and transported as provided in § 206.157.

(c)(1) Except as provided in paragraph (c)(3) of this section, for unprocessed gas valued in accordance with § 206.152 of this subpart, the transportation allowance deduction on the basis of a selling arrangement shall not exceed 50 percent of the value of the unprocessed gas determined in accordance with § 206.152 of this subpart.

(2) Except as provided in paragraph (c)(3) of this section, for gas production valued in accordance with § 206.153 of this subpart the transportation allowance deduction on the basis of a selling arrangement shall not exceed 50 percent of the value of the residue gas or gas plant product determined in accordance with § 206.153 of this subpart. For purposes of this section, natural gas liquids shall be considered one product.

(3) Upon request of a lessee, MMS may approve a transportation allowance deduction in excess of the limitations prescribed by paragraphs (c)(1) and (2) of this section. The lessee must demonstrate that the transportation costs incurred in excess of the limitations prescribed in paragraphs (c)(1) and (2) of this section were reasonable, actual, and necessary. An application for exception shall contain all relevant and supporting documentation necessary for the MMS to make a determination. Under no circumstances shall the value for royalty purposes under any selling arrangement be reduced to zero.

(d) If, after a review and/or audit, MMS determines that a lessee has improperly determined a transportation allowance authorized by this subpart, then the lessee shall pay any additional royalties, plus interest, determined in accor-

dance with 30 C.F.R. 218.54, or shall be entitled to a credit, without interest.

**§ 206.157 Determination of transportation allowances.**

(a) *Arm's-length transportation contracts.* (1)(i) For transportation costs incurred by a lessee pursuant to an arm's-length contract, the transportation allowance shall be the reasonable, actual costs incurred by the lessee for transporting the unprocessed gas, residue gas and/or gas plant products under that contract, except as provided in paragraphs (a)(1)(ii) and (iii) of this section, subject to monitoring, review, audit, and adjustment. The lessee shall have the burden of demonstrating that its contract is arm's-length. Such allowances shall be subject to the provisions of paragraph (f) of this section. Before any deduction may be taken, the lessee must submit a completed page one of Form MMS-4295 (and Schedule 1), Gas Transportation Allowance Report, in accordance with paragraph (c)(1) of this section. A transportation allowance may be claimed retroactively for a period of not more than 3 months prior to the first day of the month that Form MMS-4295 is filed with MMS, unless MMS approves a longer period upon a showing of good cause by the lessee.

(ii) In conducting reviews and audits, MMS will examine whether or not the contract reflects more than the consideration actually transferred either directly or indirectly from the lessee to the transporter for the transportation. If the contract reflects more than the total consideration, then the MMS may require that the transportation allowance be determined in accordance with paragraph (b) of this section.

(iii) If the MMS determines that the consideration paid pursuant to an arm's-length transportation contract does not reflect the reasonable value of the transportation because of misconduct by or between the contracting parties, or because the lessee otherwise has breached its duty to the lessor to market the production for the mutual

benefit of the lessee and the lessor, then MMS shall require that the transportation allowance be determined in accordance with paragraph (b) of this section. When MMS determines that the value of the transportation may be unreasonable, MMS will notify the lessee and give the lessee an opportunity to provide written information justifying the lessee's transportation costs.

(2)(i) If an arm's-length transportation contract includes more than one product in a gaseous phase and the transportation costs attributable to each product cannot be determined from the contract, the total transportation costs shall be allocated in a consistent and equitable manner to each of the products transported in the same proportion as the ratio of the volume of each product (excluding waste products which have no value) to the volume of all products in the gaseous phase (excluding waste products which have no value). Except as provided in this paragraph, no allowance may be taken for the costs of transporting lease production which is not royalty bearing without MMS approval.

(ii) Notwithstanding the requirements of paragraph (i), the lessee may propose to MMS a cost allocation method on the basis of the values of the products transported. MMS shall approve the method unless it determines that it is not consistent with the purposes of the regulations in this part.

(3) If an arm's-length transportation contract includes both gaseous and liquid products and the transportation costs attributable to each cannot be determined from the contract, the lessee shall propose an allocation procedure to MMS. The lessee may use the transportation allowance determined in accordance with its proposed allocation procedure until MMS issues its determination on the acceptability of the cost allocation. The lessee shall submit all relevant data to support its proposal. The initial proposal must be submitted by June 30, 1988, or within 3 months after the last day of the month for which the lessee requests a transportation allowance, whichever is later (unless MMS

approves a longer period). The MMS shall then determine the gas transportation allowance based upon the lessee's proposal and any additional information MMS deems necessary.

(4) Where the lessee's payments for transportation under an arm's-length contract are not based on a dollar per unit, the lessee shall convert whatever consideration is paid to a dollar value equivalent for the purposes of this section.

(5) Where an arm's-length sales contract price or a posted price includes a provision whereby the listed price is reduced by a transportation factor, MMS will not consider the transportation factor to be a transportation allowance. The transportation factor may be used in determining the lessee's gross proceeds for the sale of the product. The transportation factor may not exceed 50 percent of the base price of the product without MMS approval.

(b) *Non-arm's-length or no contract.* (1) If a lessee has a non-arm's-length transportation contract or has no contract, including those situations where the lessee performs transportation services for itself, the transportation allowance will be based upon the lessee's reasonable actual costs as provided in this paragraph. All transportation allowances deducted under a non-arm's-length or no contract situation are subject to monitoring, review, audit, and adjustment. Before any estimated or actual deduction may be taken, the lessee must submit a completed Form MMS-4295 in accordance with paragraph (c)(2) of this section. A transportation allowance may be claimed retroactively for a period of not more than 3 months prior to the first day of the month that Form MMS-4295 is filed with MMS, unless MMS approves a longer period upon a showing of good cause by the lessee. The MMS will monitor the allowance deductions to ensure that deductions are reasonable and allowable. When necessary or appropriate, MMS may

direct a lessee to modify its estimated or actual transportation allowance deduction.

(2) The transportation allowance for non-arm's-length or no-contract situations shall be based upon the lessee's actual costs for transportation during the reporting period, including operating and maintenance expenses, overhead, and either depreciation and a return on undepreciated capital investment in accordance with paragraph (b)(2)(iv)(A) of this section, or a cost equal to the initial depreciable investment in the transportation system multiplied by a rate of return in accordance with paragraph (b)(2)(iv)(B) of this section. Allowable capital costs are generally those costs for depreciable fixed assets (including costs of delivery and installation of capital equipment) which are an integral part of the transportation system.

(i) Allowable operating expenses include: Operations supervision and engineering; operations labor; fuel; utilities; materials; ad valorem property taxes; rent; supplies; and any other directly allocable and attributable operating expense which the lessee can document.

(ii) Allowable maintenance expenses include: Maintenance of the transportation system; maintenance of equipment; maintenance labor; and other directly allocable and attributable maintenance expenses which the lessee can document.

(iii) Overhead directly attributable and allocable to the operation and maintenance of the transportation system is an allowable expense. State and Federal income taxes and severance taxes and other fees, including royalties, are not allowable expenses.

(iv) A lessee may use either depreciation or a return on depreciable capital investment. After a lessee has elected to use either method for a transportation system, the lessee may not later elect to change to the other alternative without approval of the MMS.

(A) To compute depreciation, the lessee may elect to use either a straight-line depreciation method based on the life of equipment or on the life of the reserves which the transportation system services, or a unit of production method. After an election is made, the lessee may not change methods without MMS approval. A change in ownership of a transportation system shall not alter the depreciation schedule established by the original transporter/lessee for purposes of the allowance calculation. With or without a change in ownership, a transportation system shall be depreciated only once. Equipment shall not be depreciated below a reasonable salvage value.

(B) The MMS shall allow as a cost an amount equal to the allowable initial capital investment in the transportation system multiplied by the rate of return determined pursuant to paragraph (b)(2)(v) of this section. No allowance shall be provided for depreciation. This alternative shall apply only to transportation facilities first placed in service after March 1, 1988.

(v) The rate of return shall be the industrial rate associated with Standard and Poor's BBB rating. The rate of return shall be the monthly average rate as published in *Standard and Poor's Bond Guide* for the first month of the reporting period for which the allowance is applicable and shall be effective during the reporting period. The rate shall be redetermined at the beginning of each subsequent transportation allowance reporting period (which is determined pursuant to paragraph (c) of this section).

(3)(i) The deduction for transportation costs shall be determined on the basis of the lessee's cost of transporting each product through each individual transportation system. Where more than one product in a gaseous phase is transported, the allocation of costs to each of the products transported shall be made in a consistent and equitable manner in the same proportion as the ratio of the volume of each product (excluding waste products which have no

value) to the volume of all products in the gaseous phase (excluding waste products which have no value). Except as provided in this paragraph, the lessee may not take an allowance for transporting a product which is not royalty bearing without MMS approval.

(ii) Notwithstanding the requirements of paragraph (i), the lessee may propose to the MMS a cost allocation method on the basis of the values of the products transported. MMS shall approve the method unless it determines that it is not consistent with the purposes of the regulations in this part.

(4) Where both gaseous and liquid products are transported through the same transportation system, the lessee shall propose a cost allocation procedure to MMS. The lessee may use the transportation allowance determined in accordance with its proposed allocation procedure until MMS issues its determination on the acceptability of the cost allocation. The lessee shall submit all relevant data to support its proposal. The initial proposal must be submitted by June 30, 1988 or within 3 months after the last day of the month for which the lessee begins the transportation, whichever is later, unless MMS approves a longer period. The MMS shall then determine the transportation allowance based upon the lessee's proposal and any additional information MMS deems necessary.

(5) A lessee may apply to the MMS for an exception from the requirement that it compute actual costs in accordance with paragraphs (b)(1) through (b)(4) of this section. The MMS will grant the exception only if the lessee has a tariff for the transportation system approved by the Federal Energy Regulatory Commission (FERC) (for both Federal and Indian leases) or a state regulatory agency (for Federal leases). The MMS shall deny the exception request if it determines that: (i) The tariff is excessive as compared to arm's-length transportation charges by the lessee or others providing similar transportation services; or (ii) if

there are no arm's-length transportation charges by the lessee or others providing similar transportation services, the tariff significantly exceeds the lessee's actual costs for transportation as determined under this section.

(c) *Reporting requirements—(1) Arm's-length contracts.* (i) With the exception of those transportation allowances specified in paragraphs (c)(1)(v) and (vi) of this section, the lessee shall submit page one of the initial Form MMS-4295 (and Schedule 1) prior to, or at the same time as, the transportation allowance determined pursuant to an arm's-length contract is reported on Form MMS-2014, Report of Sales and Royalty Remittance. A Form MMS-4295 received by the end of the month that the Form MMS-2014 is due shall be considered to be timely received.

(ii) The initial Form MMS-4295 shall be effective for a reporting period beginning the month that the lessee is first authorized to deduct a transportation allowance and shall continue until the end of the calendar year, or until the applicable contract or rate terminates or is modified or amended, whichever is earlier.

(iii) After the initial reporting period and for succeeding reporting periods, lessees must submit page one of Form MMS-4295 (and Schedule 1) within 3 months after the end of the calendar year, or after the applicable contract or rate terminates or is modified or amended, whichever is earlier, unless MMS approves a longer period (during which period the lessee shall continue to use the allowance from the previous reporting period).

(iv) The MMS may require that a lessee submit arm's-length transportation contracts, production agreements, operating agreements, and related documents. Documents shall be submitted within a reasonable time, as determined by MMS.

(v) Transportation allowances which are based on arm's-length contracts and which are in effect at the time these

regulations become effective will be allowed to continue until such allowances terminate. For the purposes of this section, only those allowances that have been approved by MMS in writing shall qualify as being in effect at the time these regulations become effective.

(vi) The MMS may establish, in appropriate circumstances, reporting requirements which are different from the requirements of this section.

(2) *Non-arm's-length or no contract.* (i) With the exception of those transportation allowances specified in paragraphs (c)(2)(v), (c)(2)(vii), and (c)(2)(viii) of this section, the lessee shall submit an initial Form MMS-4295 prior to, or at the same time as, the transportation allowance determined pursuant to a non-arm's-length contract or no-contract situation is reported on Form MMS-2014, Report of Sales and Royalty Remittance. A Form MMS-4295 received by the end of the month that the Form MMS-2014 is due shall be considered to be timely received. The initial report may be based upon estimated costs.

(ii) The initial Form MMS-4295 shall be effective for a reporting period beginning the month that the lessee first is authorized to deduct a transportation allowance and shall continue until the end of the calendar year, or until the transportation under the non-arm's-length contract or the no contract situation terminates, whichever is earlier.

(iii) For calendar-year reporting periods succeeding the initial reporting period, the lessee shall submit a completed Form MMS-4295 containing the actual costs for the previous reporting period. If the transportation is continuing, the lessee shall include on Form MMS-4295 its estimated costs for the next calendar year. The estimated transportation allowance shall be based on the actual costs for the previous reporting period plus or minus any adjustments which are based on the lessee's knowledge of decreases or increases which will affect the allowance. Form

MMS-4295 must be received by MMS within 3 months after the end of the previous reporting period, unless MMS approves a longer period (during which period the lessee shall continue to use the allowance from the previous reporting period).

(iv) For new transportation facilities or arrangements, the lessee's initial Form MMS-4295 shall include estimates of the allowable transportation costs for the applicable period. Cost estimates shall be based upon the most recently available operations data for the transportation system, or if such data are not available, the lessee shall use estimates based upon industry data for similar transportation systems.

(v) Non-arm's-length contract or no contract based transportation allowances which are in effect at the time these regulations become effective will be allowed to continue until such allowances terminate. For the purposes of this section, only those allowances that have been approved by MMS in writing shall qualify as being in effect at the time these regulations become effective.

(vi) Upon request by MMS, the lessee shall submit all data used to prepare its Form MMS-4295. The data shall be provided within a reasonable period of time, as determined by MMS.

(vii) The MMS may establish in appropriate circumstances, reporting requirements which are different from the requirements of this section.

(viii) If the lessee is authorized to use its FERC-approved tariff as its transportation cost in accordance with subsection (b)(5) of this section, it shall follow the reporting requirements of subsection (c)(1) of this section.

(3) The MMS may establish reporting dates for individual lessees different than those specified in this subpart in order to provide more effective administration.

Lessees will be notified of any change in their reporting period.

(4) Transportation allowances must be reported as a separate line item on Form MMS-2014, unless MMS approves a different reporting procedure.

(d) *Interest assessments for incorrect or late reports and failure to report.* (1) If a lessee deducts a transportation allowance on its Form MMS-2014 without complying with the requirements of this section, the lessee shall pay interest only on the amount of such deduction until the requirements of this section are complied with. The lessee also shall repay the amount of any allowance which is disallowed by this section.

(2) If a lessee erroneously reports a transportation allowance which results in an underpayment of royalties, interest shall be paid on the amount of that underpayment.

(3) Interest required to be paid by this section shall be determined in accordance with 30 C.F.R. 218.54.

(e) *Adjustments.* (1) If the actual transportation allowance is less than the amount the lessee has estimated and taken during the reporting period, the lessee shall be required to pay additional royalties due, plus interest computed pursuant to 30 C.F.R. 218.54, retroactive to the first month the lessee is authorized to deduct a transportation allowance. If the actual transportation allowance is greater than the amount the lessee has estimated and taken during the reporting period, the lessee shall be entitled to a credit without interest.

(2) For lessees transporting production from onshore Federal and Indian leases, the lessee must submit a corrected Form MMS-2014 to reflect actual costs, together with any payment, in accordance with instructions provided by MMS.

(3) For lessees transporting gas production from leases on the OCS, if the lessee's estimated transportation allow-

ance exceeds the allowance based on actual costs, the lessee must submit a corrected Form MMS-2014 to reflect actual costs, together with its payment, in accordance with instructions provided by MMS. If the lessee's estimated transportation allowance is less than the allowance based on actual costs, the refund procedure will be specified by MMS.

(f) *Actual or theoretical losses.* Notwithstanding any other provisions of this subpart, for other than arm's-length contracts no cost shall be allowed for transportation which results from payments (either volumetric or for value) for actual or theoretical losses. This section does not apply when the transportation allowance is based upon a FERC or state regulatory agency approved tariff.

(g) *Other transportation cost determinations.* The provisions of this section shall apply to determine transportation costs when establishing value using a net-back valuation procedure or any other procedure that requires deduction of transportation costs.

**§ 206.158 Processing allowances–general.**

(a) Where the value of gas is determined pursuant to § 206.153 of this subpart, a deduction shall be allowed for the reasonable actual costs of processing.

(b) Processing costs must be allocated among the gas plant products. A separate processing allowance must be determined for each gas plant product and processing plant relationship. Natural gas liquids (NGL's) shall be considered as one product.

(c)(1) Except as provided in paragraph (d)(2) of this section, the processing allowance shall not be applied against the value of the residue gas. Where there is no residue gas MMS may designate an appropriate gas plant product against which no allowance may be applied.

(2) Except as provided in paragraph (c)(3) of this section, the processing allowance deduction on the basis of an

individual product shall not exceed 664 2/3 percent of the value of each gas plant product determined in accordance with § 206.153 of this subpart (such value to be reduced first for any transportation allowances related to postprocessing transportation authorized by § 206.156 of this subpart).

(3) Upon request of a lessee, MMS may approve a processing allowance in excess of the limitation prescribed by paragraph (c)(2) of this section. The lessee must demonstrate that the processing costs incurred in excess of the limitation prescribed in paragraph (c)(2) of this section were reasonable, actual, and necessary. An application for exception shall contain all relevant and supporting documentation for MMS to make a determination. Under no circumstances shall the value for royalty purposes of any gas plant product be reduced to zero.

(d)(1) Except as provided in paragraph (d)(2) of this section, no processing cost deduction shall be allowed for the costs of placing lease products in marketable condition, including dehydration, separation, compression, or storage, even if those functions are performed off the lease or at a processing plant. Where gas is processed for the removal of acid gases, commonly referred to as "sweetening," no processing cost deduction shall be allowed for such costs unless the acid gases removed are further processed into a gas plant product. In such event, the lessee shall be eligible for a processing allowance as determined in accordance with this subpart. However, MMS will not grant any processing allowance for processing lease production which is not royalty bearing.

(2)(i) If the lessee incurs extraordinary costs for processing gas production from a gas production operation, it may apply to MMS for an allowance for those costs which shall be in addition to any other processing allowance to which the lessee is entitled pursuant to this section. Such an allowance may be granted only if the lessee can demonstrate that the costs are, by reference to standard industry condi-

tions and practice, extraordinary, unusual, or unconventional.

(ii) Prior MMS approval to continue an extraordinary processing cost allowance is not required. However, to retain the authority to deduct the allowance the lessee must report the deduction to MMS in a form and manner prescribed by MMS.

(e) If MMS determines that a lessee has improperly determined a processing allowance authorized by this subpart, then the lessee shall pay any additional royalties, plus interest determined in accordance with 30 C.F.R. 218.54, or shall be entitled to a credit, without interest.

No. 05-669

Supreme Court, U.S.
FILED
MAR 27 2006
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IN THE

# Supreme Court of the United States

BP AMERICA PRODUCTION COMPANY AND ATLANTIC RICHFIELD COMPANY,
*Petitioners,*

v.

REJANE BURTON, ACTING ASSISTANT SECRETARY OF LAND AND MINERALS MANAGEMENT, DEPARTMENT OF THE INTERIOR FOR LAND, *et al.*,
*Respondents.*

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit**

## REPLY BRIEF FOR PETITIONERS

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## REPLY FOR PETITIONERS

The United States, joined by *amicus curiae* Jicarilla Apache Nation (the "Tribe"), agrees that the second question presented by the petition warrants this Court's review. It is common ground among the parties that the courts of appeals are divided on whether the statute of limitations codified at 28 U.S.C. § 2415(a) applies to the commencement of administrative proceedings. See Gov't Br. 19; Tribe Br. 6; Pet. 27. It is likewise common ground that that question is both important and recurring. As the United States (Br. 21) and the Tribe (Br. 7) explain, the issue affects thousands of leases for oil and gas and other minerals on Indian lands; numerous federal leases for minerals other than oil and gas; and a variety of other monetary disputes between private parties and the government. See also Pet. 30. In each of those contexts, the statute of limitations for bringing an administrative complaint—indeed, whether there is any limitations period at all—now depends wholly on the circuit in which the matter is eventually litigated. This Court should grant the petition and restore uniformity to this important area of law.

Contrary to respondents' position, however, the first question presented by the petition also warrants this Court's review. The Mineral Leasing Act of 1920 ("MLA"), 41 Stat. 437, codified at 30 U.S.C. § 181 *et seq.*, provides for the payment of royalties based on the "amount or value of production removed or sold from the lease." 30 U.S.C. § 226(b)(2)(A)(ii). The decision below holds that the MLA's text requires only that leasehold production subject to the royalty *originate* at the lease, so that royalties on such production can be based on the much higher value the production will have once it is transported to off-lease locations and improved in quality to finished, end-use condition. That construction is in direct conflict with decisions from the Ninth Circuit and prior decisions from the D.C. Circuit, which have held that the MLA imposes a "statutory

mandate" that royalty payments be based on the value of production *at the lease*. Pet. 17-18.

Like the statute of limitations issue, the construction of the MLA is an exceedingly important and recurring issue. The construction of the MLA affects the same leases as the statute of limitations issue—Indian leases and leases for minerals other than oil and gas—as well as thousands of additional federal oil and gas leases. These leases generate several billion dollars in royalties per year. Pet. 23; Gov't Br. 20-21.

## I. The Court Should Resolve The Circuit Split Over The Meaning Of 28 U.S.C. § 2415(a).

### A. Whether The Statute Of Limitations In 28 U.S.C. § 2415(a) Applies To Agency Orders Mandating The Payment Of Money Is Of Recurring Importance In Many Contexts.

The decision below expressly acknowledged that its holding directly conflicts with the decisions of other circuits. Pet. App. 18a. In this case, the D.C. Circuit joined the Fifth Circuit, see *Phillips Petroleum Co.* v. *Johnson*, No. 93-1377, 1994 WL 484506 (5th Cir. Sept. 7, 1994), in holding that the statute of limitations codified at 28 U.S.C. § 2415(a) does not apply to agency actions. Pet. 16a-20a. The Tenth Circuit and Federal Circuit have reached the opposite result. See *OXY USA, Inc.* v. *Babbitt*, 268 F.3d 1001 (10th Cir. 2001); *United States* v. *Hanover Ins. Co.*, 82 F.3d 1052 (Fed. Cir. 1996); see also Pet. 26. Like the court of appeals, respondents and the Tribe acknowledge the conflict. Gov't Br. 19; Tribe Br. 6-7.

The parties also agree that the issue is of such prospective importance that it warrants this Court's review. The United States, for example, notes that whether Section 2415(a) applies to royalties continues to arise in the context of Indian mineral leases and federal mineral leases other than oil and gas. Gov't Br. 21. In fiscal year 2005, those

leases generated over $1 billion in royalties. Gov't Br. 21; see also Tribe Br. 18; Pet. 30. The Court should therefore grant the petition and resolve the conflict among the courts of appeals on this issue.

**B. The Limitations Period In 28 U.S.C. § 2415(a) Applies To Agency Orders Mandating The Payment Of Money.**

Although respondents agree that the Court should grant review, they devote much of their brief to defending the decision below on the merits. Respondents begin by arguing that Section 2415(a)'s references to an "action for money damages" and a "complaint" connote judicial actions rather than administrative actions. Gov't Br. 15. That argument overlooks that Section 2415(a) does not simply refer to an "action for money damages" but to "*every* action for money damages." 28 U.S.C. § 2415(a) (emphasis added). As the Tenth Circuit observed, the reference to actions for money damages found in Section 2415 is "patently broad" and sufficient to encompass actions brought in both administrative and judicial forums. *OXY USA*, 268 F.3d at 1005. Furthermore, Congress has frequently used the term "complaint" in a variety of statutes to describe efforts to recover monetary compensation through administrative proceedings. See, *e.g.*, 15 U.S.C. § 45(b); 15 U.S.C. § 522; 25 U.S.C. § 2713; 29 U.S.C. § 160(b).

Respondents also argue that Section 2415(a), by its terms, provides that administrative proceedings will *extend* the time for filing in court, but that Section 2415(a) contains no limit on when an administrative proceeding may be initiated. Gov't Br. 16. That interpretation of Section 2415(a) cannot be reconciled with Congress's intent to have Section 2415(a) function as a broad, catch-all limitations period. *OXY*, 268 F.3d at 1005. As the Federal Circuit has explained, Congress could not have intended "agencies to be free to assert their claims at any time and by any means

other than court actions, unencumbered by the period of limitation imposed by section 2415(a)." *Hanover Ins. Co.*, 82 F.3d at 1055.

Respondents, moreover, do not dispute that their construction converts a provision of Section 2415(a) into mere surplusage. Gov't Br. 16. Subsection (i) of Section 2415 expressly states that administrative offsets are exempt from the limitations period imposed by Section 2415(a). If Section 2415(a) did not apply to administrative actions, then there would be no need to carve out a select type of administrative action from Section 2415(a). *OXY*, 268 F.3d at 1006. This Court, of course, will avoid any interpretation that renders even a word or phrase—much less an entire subsection—superfluous. *United States* v. *Menasche*, 348 U.S. 528, 538-539 (1955); *Pennsylvania Dep't of Pub. Welfare* v. *Davenport*, 495 U.S. 552, 562 (1990) ("Our cases express a deep reluctance to interpret a statutory provision so as to render superfluous other provisions in the same enactment."); see also *Department of Revenue of Or.* v. *ACF Indus.*, 510 U.S. 332, 340 (1994) (rejecting result that "would contravene the elementary canon of construction that a statute should be interpreted so as not to render one part inoperative") (internal quotation marks omitted).

While respondents attempt to escape the import of subsection (i) by relying on legislative history, Gov't Br. 16-17, this Court does "not resort to legislative history to cloud a statutory text that is clear." *Ratzlaf* v. *United States*, 510 U.S. 135, 147-148 (1994) (footnote omitted). Moreover, even if it were relevant, "[t]he legislative history in support of § 2415(a) indicates Congress was motivated * * * to reduce the costs of record keeping and encourage prompt agency actions on claims." *Phillips Petroleum Co.* v. *Lujan*, 4 F.3d 858, 863 (10th Cir. 1993).

### C. MMS Orders To Pay Royalties Seek Money Damages Founded On Contract.

Respondents argue that, even if Section 2415 applies to agency orders mandating the payment of money, Section 2415 does not apply to MMS orders to pay royalties. According to respondents, such orders do not seek the payment of "money damages" and are not based upon a contract. Respondents are mistaken on both counts.

The lower courts have long recognized that oil and gas leases are contracts. *OXY*, 268 F.3d at 1007-1008; *Phillips Petroleum Co.*, 4 F.3d at 860-861 & n. 1; *Reese Exploration, Inc.* v. *Williams Natural Gas*, 983 F.2d 1514, 1518-1519 (10th Cir. 1993). Indeed, the District Court below conceded that "the MMS order was based upon a contract * * * ." Pet. 54a. That comports with common sense. Absent a contractual agreement to pay royalties, the MMS would have no right to demand a royalty at all. The claim for money is thus founded on contract.

The fact that the MMS administers federal oil and gas leases in accordance with the MLA does not change the analysis. The legal source of the right to a royalty payment is the lease, not the statutes and regulations that govern the MMS's administration of the lease. The MMS's own rules make it clear that the contract is not a mere formality or an incident to governing rules and regulations. Where the terms of a lease are inconsistent with the regulations, the terms of the lease rather than the regulations govern the government's royalty rights. See 30 C.F.R. § 202.100(b)(3).

The United States cites one case to support its position that an action for past-due sums under an MMS lease is not an action for damages. That case, *Bowen* v. *Massachusetts*, 487 U.S. 879, 900 (1988), considered whether a suit seeking to enforce a statutory mandate, which happened to be one for the payment of money, was a suit for "money damages." The MMS orders here, however, did not seek to enforce a

statutory mandate. They sought money MMS believed to be due under a contract. That effort to recover past-due money under a lease is a paradigmatic suit for money damages founded on contract. See, *e.g.*, Corbin on Contracts § 55.6 (Interim Ed. 2005) (stating that the remedy of "damages" is an amount determined "with the purpose of putting the injured party in as good a position as that party would have occupied had the contract been fully performed by the defendant"). As the Tenth Circuit observed, an MMS claim to collect royalties is "substantively indistinguishable from other government claims to recover money owed under contracts governed by the limitations period in [Section] 2415." *OXY*, 268 F.3d at 1008.

## II. The Court Also Should Address The Proper Construction Of The MLA.

### A. The Courts Are Divided On Whether The MLA Requires Royalties To Be Based On The Value Of Production At The Geographic Location Of The Lease.

Under the MLA, federal lessees of mineral producing lands must pay royalties based on the "amount or value of the production removed or sold from the lease." 30 U.S.C. § 226(b)(1)(A). The Ninth Circuit and prior decisions of the D.C. Circuit have all recognized that the statutory phrase "amount or value of production * * * from the lease" means the amount or value of production at the geographic location of the lease. In conflict with those decisions, the decision below holds that the statute requires only that production originate at the lease—so that royalties can be based on the greater value of production that has been transported significant distances to off-lease locations and improved in quality to finished, end-use condition.

Long-established precedent from the Ninth Circuit holds that royalty values are to be determined at the wellhead point of production from the lease. See *United States* v.

*Gen. Petroleum Corp.*, 73 F. Supp. 225, 254 (S.D. Cal. 1947) ("Natural-gas royalties are payable on the gas as it is produced *at the well*. It is the value of that gas which must be determined.") (emphasis added), aff'd, *Continental Oil Co.* v. *United States*, 184 F.2d 802, 820 (9th Cir. 1950) (royalties are "calculated values *at the wells* not at the pipe line destination") (emphasis added). The same precedent makes clear that, when costs are incurred to enhance the value of the production above the value of production at the lease, allowances must be made for the costs "in order to arrive at the value of the gas as originally produced." 73 F. Supp. at 254. Respondents try to distinguish those cases by ignoring the statutory construction issue and asserting that the Ninth Circuit did not address "whether gas was in marketable condition." Gov't Br. 14. But the Ninth Circuit squarely addressed the statutory interpretation question and declared that royalty values must be determined based on the production's market value at the wellhead point of production from the lease. See also *Marathon Oil Co.* v. *United States*, 604 F. Supp. 1375, 1386 (D. Alaska 1985) (holding that the statutory reference to "value of production" requires that "royalties be based on the value of production *at the lease*") (emphasis in original), aff'd, 807 F.2d 759, 765-766 (9th Cir. 1986).

The D.C. Circuit's decision in *Independent Petroleum Ass'n of America* v. *DeWitt*, 279 F.3d 1036 (D.C. Cir. 2002), is to the same effect. In *DeWitt*, consistent with *General Petroleum* and *Marathon Oil*, the D.C. Circuit observed that "to abide by the *statutory mandate* to base royalty on the 'value of the production removed or sold from the lease,'" the agency allows deductions "when production is sold at a market away from the lease." 279 F.3d at 1037 (emphasis added). The *DeWitt* court's reference to deductions when production is sold at markets away from the lease under a "statutory mandate" makes sense only if the

statutory mandate is for royalty *valuation* at the lease, not that the production merely *originate* at the lease.

Here, the decision below reached the opposite result, holding that the MLA may be construed to mean that production need only originate at the lease, such that the agency may demand royalties based on the greatly enhanced value of production after it has been transported to off-lease facilities and improved in quality to finished, end-use condition. This Court should grant the petition to resolve this conflict of statutory interpretation among the courts.

### B. The MMS's Own Regulations Require Royalties To Be Based On The Value Of Production At The Geographic Location Of The Lease.

1. The Department of Interior's regulations also require that royalties be based on the value of production at the geographic location of the lease.[1] That was the expressed intent of the MMS in the 1988 rulemaking that adopted the regulations at issue here. In its rulemaking, the MMS noted that it had been "MMS policy since 1961 to grant transportation allowances when production is moved to a sales point off the lease *in order to calculate the value of the product at the lease*." 53 Fed. Reg. 1230, 1257 (Jan. 15, 1988) (emphasis added). Pet. 21. The regulations do provide that valuations at the lease may be *derived* from sales or valuations at off-lease locations downstream from the lease. But where production is sold or valued based on market prices downstream from the lease, the MMS's regulations specify that the costs of "transportation, pro-

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[1] As one court has observed, the longstanding interpretation of the statutory value of production "recognized by Interior" and "affirmed by the courts" is that "it refers to the value of oil or gas *at the wells*." *Indep. Petroleum Ass'n of Am.* v. *Armstrong*, 91 F. Supp. 2d 117, 125 (D.D.C. 2000), rev'd in part, aff'd in part, *Indep. Petroleum Ass'n of Am.* v. *DeWitt*, 279 F.3d 1036 (D.C. Cir. 2002).

cessing or manufacturing" are deducted in order to calculate a "net-back" or "work-back" value of production *at the lease*. 30 C.F.R. § 206.151; Pet. 21.

As respondents note, petitioner Amoco sold its production at the wellhead to a marketing affiliate and calculated royalty payments from third-party sales proceeds received by the affiliate at off-lease sales locations, reduced by costs incurred to transport and condition the production between the lease and the off-lease sales points. Gov't Br. 3.[2] That is the precise "net-back" or "work-back" method for "calculating market values of gas *at the lease*" that is specified by the regulations. 30 C.F.R. § 206.151 (emphasis added). To deny allowances for such costs results in royalty obligations that greatly exceed the value of production *at the lease*. Even if the MLA did not compel a royalty valuation at the lease, the agency cannot change the requirement of royalty valuation at the lease specified by its current regulations without a notice-and-comment rulemaking. *Fina Oil and Chem. Co.* v. *Norton*, 332 F.3d 672, 679 (D.C. Cir. 2003).

2. As respondents observe (Br. 9), MMS regulations also require that the lessee incur any costs required to "place gas in marketable condition" (30 C.F.R. § 206.152 (i)) and define gas in "marketable condition" as gas that is "sufficiently free from impurities and otherwise in a condition that [it] will be accepted by a purchaser under a sales contract typical for the field or area." 30 C.F.R. § 206.151. The court of appeals reasoned that petitioners could be required to incur off-lease costs under the marketable condition rule, because "[t]he regulation stipulating that producers are to place gas in marketable condition at no cost to the government does not contain a geographic element." Pet. 10a. That construction, however, cannot be reconciled with other regulations requiring that both the quantity and quality of

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[2] Both Amoco's sales prices at the wellhead and its royalty payments to the government were derived from market-value third-party sales received by Amoco's marketing affiliate.

production be measured *at the lease*. Pet. 20-22. Consistent with a correct construction of the MLA as requiring royalty valuations at the lease, where a producer sells its production for market value at the lease—as is the case here—that gas satisfies the marketable condition rule. Gov't Br. 3. *California Co.* v. *Udall*, 296 F.2d 384 (D.C. Cir. 1961) (gas is in marketable condition where it meets quality standards for sales under wellhead sales contracts); *Amerada Hess Corp.* v. *DOI*, 170 F.3d 1032, 1037 (10th Cir. 1999) (the marketable condition rule is inapplicable if the gas is marketable in the condition as it exists at or within a short distance of the well). Pet. 18-20. The fact that downstream purchasers may process the gas further and transport it to different geographic markets does not mean that the gas was somehow in unmarketable condition when it was sold in industry-standard condition at the lease or well-head.

## CONCLUSION

For the foregoing reasons and those stated in the petition, the petition for a writ of certiorari should be granted.

Respectfully submitted.

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No. 05-669

IN THE

# Supreme Court of the United States

BP America Production Company and
Atlantic Richfield Company,
*Petitioners*,

v.

Rebecca W. Watson,
Assistant Secretary of the Interior for Land
and Mineral Management, *et al.*,
*Respondents*.

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit**

## BRIEF OF *AMICUS CURIAE* JICARILLA APACHE NATION IN SUPPORT OF PETITIONERS ON THE STATUTE OF LIMITATIONS QUESTION ONLY

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## QUESTION PRESENTED

Whether the statute of limitations in 28 U.S.C. § 2415(a), which applies to "every *action for money damages* brought by the United States" and bars such actions "unless the *complaint* is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings . . . , whichever is later," applies to *administrative orders* of the Minerals Management Service requiring oil and gas companies to *pay additional royalties* and granting them a right to appeal *within the agency*, a question as to which the courts of appeals are in conflict.

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**On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit**

## BRIEF OF *AMICUS CURIAE* JICARILLA APACHE NATION IN SUPPORT OF PETITIONERS ON THE STATUTE OF LIMITATIONS QUESTION ONLY

The Jicarilla Apache Nation ("tribe") respectfully submits this brief as *amicus curiae* in support of petitioners BP America Production Company and Atlantic Richfield Company for a writ of certiorari on the statute of limitations question only; the tribe does not support petitioners' request for a writ of certiorari on the question of marketable condition. [1]

[1] No counsel for any party authored any portion of this brief and no person or entity other than the *amicus curiae* made a monetary contribution to the preparation or submission of this brief. All parties to this case have consented to the filing of this brief, as indicated in letters filed with the Court.

## INTEREST OF *AMICUS CURIAE*

The Jicarilla Apache Nation is a federally recognized Indian tribe located in northwest New Mexico on the eastern edge of the San Juan Basin, which is the second largest natural gas field in the lower 48 states. The tribe is the lessor and royalty owner of over 100 oil and gas mining leases issued under the Indian Mineral Leasing Act of 1938, 25 U.S.C. §§ 396a-396g (2000). Royalties from oil and gas production on these leases provide about half of all the revenue used to pay for essential government services on the tribe's reservation.

Lessees on Indian and federal lands initially pay royalties based on their own reports of the volume and value of their oil and gas production. If and when audits of these reports are performed, in many instances the audits reveal that significant additional royalties are due. In those instances the Minerals Management Service ("MMS"), the agency in the Department of the Interior responsible for managing federal and Indian oil and gas royalties, issues orders to the oil and gas production companies requiring them to pay additional royalties to the lessor. Several such orders involving oil and gas produced from the Jicarilla Apache Reservation are on appeal before the MMS. In addition, the tribe is currently participating in or anticipates audits of other royalty issues.

These pending appeals and audits involve periods that stretch back more than six years from the date of the relevant MMS orders. If these proceedings are considered by the D.C. Circuit, where MMS is located, the tribe can receive additional royalties for the entire period at issue in each case, since the D.C. Circuit has found that the six-year statute of limitations in 28 U.S.C. § 2415(a) (2000) does not apply to administrative orders directing additional payments of royalties. If the proceedings are considered by the Tenth Circuit, however,

where the Jicarilla Apache Reservation is located, additional royalties due for periods more than six years from the dates of the relevant orders will not be collectible from the oil and gas companies. The amounts at issue are in the tens of millions of dollars and, if rendered uncollectible, will result in a windfall to the oil and gas companies: they will be rewarded for underreporting the amount of royalties they owed to the tribe. The Jicarilla Apache Nation therefore has a significant and substantial interest in the Court resolving the split in the circuits regarding the applicability of § 2415(a) to MMS orders for payment of additional royalties.

## SUMMARY OF ARGUMENT

Petitioner oil and gas companies have asked this Court to grant a writ of certiorari on two questions, the statute of limitations and the proper royalty treatment of the costs of placing coalbed methane gas into marketable condition. The Jicarilla Apache Nation supports the petition for a writ of certiorari on the statute of limitations: this question is the subject of a split among at least three federal courts of appeals and has a substantial financial impact not only for the Jicarilla Apache Nation but also for other oil- and gas-owning tribes. The Jicarilla Apache Nation opposes certiorari on the marketable condition question for the reasons articulated in respondent United States' brief, and does not repeat those arguments here.

## ARGUMENT

### I. The Court Should Grant the Petition on the Statute of Limitations in Order to Clarify the Law on this Question and Uphold the D.C. Circuit's Decision, Which is Consistent With the Fifth Circuit but Contrary to the Tenth Circuit.

The decision below, *Amoco Production Co. v. Watson*, 410 F.3d 722 (D.C. Cir. 2005) (Pet'r App. 1a), held that the six-year statute of limitations in 28 U.S.C. § 2415(a) (2000) does not apply to MMS orders to oil and gas producers to pay additional royalties under their leases. Section 2415(a) (Pet'r App. 179a) provides:

> every *action for money damages* brought by the United States . . . which is founded upon any contract . . . shall be barred unless the *complaint* is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings . . . , whichever is later.

(Emphasis added.) The D.C. Circuit explained that:

> [t]he phrase 'action for money damages' points strongly to a suit in a court of law, rather than an agency enforcement order that happens to concern money under a statutory scheme . . . . Any doubt is removed by the fact that subsection 2415(a) measures the limitations period from the filing of a 'complaint.' It strains legal language to construe this administrative compliance order as a

> 'complaint' for money damages in any ordinary sense of the term.

410 F.3d at 733 (Pet'r App. 16a-17a). The D.C. Circuit therefore "join[ed] the Fifth Circuit, *see Phillips Petroleum Co. v. Johnson,* No. 93-1377, 1994 WL 484506 (5th Cir. Sept. 7, 1994)," in concluding that § 2415(a) does not apply to MMS orders for the payment of additional royalties, because they are not "action[s] . . . initiated by the filing of a complaint." 410 F.3d at 734-35 (Pet'r App. 20a.)

The Fifth Circuit found that such MMS orders not only are not "actions," but also are not actions "for money damages." It held that "[t]he term 'action for money damages' refers to a suit in court seeking compensatory damages." *Id.* at *1. According to the Fifth Circuit, the MMS orders were not "actions" since no complaint was filed, and they were not for "money damages" since royalties are not compensatory but are instead an obligation under the lease.[2]

In contrast, the Tenth Circuit in *OXY USA, Inc. v. Babbitt*, 268 F.3d 1001 (2001) (*en banc*), held that an MMS order to pay additional royalties is an "action" under § 2415(a). The Tenth Circuit based its decision on its interpretation of the purpose behind the statute, 268 F.3d at 1005-6, rather than on the plain language of the statute, *id.* at 1009-12 (Briscoe, J.,

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[2]Unpublished decisions of the Fifth Circuit issued before January 1, 1996 are precedent, although they "should normally be cited only when the doctrine of res judicata, collateral estoppel or law of the case is applicable." Fifth Circuit Rule 47.5.3. In *Phillips*, however, the court stated that it issued the decision specifically to address the statute of limitations, which was "an issue that we inadvertently omitted from our previous opinion," and also stated that "[t]his supplemental opinion modifies our opinion issued on June 10, 1994" and published at 22 F.3d 616. 1994 WL 484506 at *1.

dissenting). The Tenth Circuit went on to hold that oil and gas leases are contracts, so that the MMS orders are "founded on contract," *id.* at 1006-7, and that an order to pay money under the leases is equivalent to a breach of contract action and is therefore an action for "money damages," *id.* at 1008.

Although there is now a separate seven-year statute of limitations that applies to MMS orders for payment of royalties on oil and gas produced from federal lands, as the D.C. Circuit noted, 410 F.3d at 732 n.1 (Pet'r App. 16a), *see* § 4 of the Federal Oil and Gas Royalty Simplification and Fairness Act of 1996, Pub. L. No. 104-185, 110 Stat. 1700 ("RSFA"), 30 U.S.C. § 1724 (2000), RSFA states that this provision "shall not apply with respect to Indian lands," RSFA § 9, 30 U.S.C. § 1701 note (2000), App. 8a. The split among the circuits on the applicability of the six-year statute of limitations therefore continues to have a substantial impact on the collection of royalties from Indian lands.[3] Many of the oil- and gas-producing tribes, including the Jicarilla Apache Nation, are located within the Tenth Circuit, and so are at risk of losing substantial revenues. Moreover, the split in the circuits may lead to different results for different tribes, depending on where the tribes are located and where royalty orders are litigated, thereby encouraging forum-shopping and races to the courthouse on the part of both tribes and lessee oil and gas companies.

Further, the question whether § 2415(a) applies to the issuance of administrative orders arises in contexts other than orders to pay oil and gas royalties, thus drawing more courts of

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[3] Royalties from Indian leases constituted more than 10% of total royalties from federal and Indian onshore oil and gas in 2005, and have consistently been at that level for at least the past ten years. *See* MMS Website, http://www.mrm.mms.gov/MRMWebStats/default.aspx.

appeals into the conflict. *See, e.g., United States v. Hanover Ins. Co.*, 82 F.3d 1052 (Fed. Cir. 1996) (applying § 2415(a) to Customs Service demand for payment); *King v. Railroad Retirement Bd.*, 981 F.2d 365, 367 (8th Cir. 1992) (refusing to apply § 2415(a) to Board proceeding to recover overpayment of disability benefits). The Court should grant the petition to resolve this conflict.

## II. Applying the Six-Year Statute of Limitations to MMS Orders to Pay Royalties Results in a Windfall to the Oil and Gas Industry and Decreased Revenues for the Jicarilla Apache Nation and Other Tribes.

There are substantial royalties owing to the Jicarilla Apache Nation for periods that go back more than six years from the date of issuance of the relevant MMS orders. For example, in 1998 MMS issued "major portion" orders for Jicarilla leases for the period 1985-1995. Several of these orders are pending on appeal before the MMS, and the tribe is owed over $70 million in royalties from the oil and gas industry pursuant to these orders.[4] The tribe also is still investigating

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[4] A "major portion" order refers to § 3(c) of the standard BIA Indian Lease Form 157, which provides:

> "value" for the purposes hereof [the calculation of royalties] may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered . . . at the time of production for the major portion of the oil of the same gravity, and gas . . . produced and sold from the field where the leased lands are situated.

*See also* 30 C.F.R. § 206.152(a)(3)(ii) (1988). The MMS major portion orders required oil and gas producers to re-calculate royalties owed to the tribe based on the major portion price determined by MMS and set forth in

(continued...)

some of the instances of underreporting that occurred in the past, discussed below, which may call for MMS to issue additional orders that go back more than six years. These past-due royalties result from a combination of factors: pervasive underreporting of royalties by the oil and gas industry; MMS's failure to adequately administer and enforce tribal lease provisions; and the nature of the audit process, which by definition is retroactive.

### A. Tribes are Owed Substantial Revenues Dating Back More Than Six Years Because of the Oil and Gas Industry's Long-Standing Practice of Underpaying Royalties.

The oil and gas industry has a long history of underpaying royalties to Indian tribes. *See generally* Report of the Commission, Fiscal Accountability of the Nation's Energy Resources (Jan. 1982) ("Linowes Commission Report") (selected portions at App. 1a - 7a). Twenty-five years ago, after public outrage over allegations of royalty underpayment, fraud and outright theft, the Secretary of Interior established the Linowes Commission to investigate "serious allegations of massive irregularities in royalty payments due the Federal government, Indian tribes, and States." *Id.* (Letter from David Linowes to Secretary James G. Watt (January 21, 1982)), App. 1a. After an extensive investigation, the Linowes Commission concluded:

> Management of royalties for the nation's energy resources has been a failure for more than 20 years. Because the Federal government has not adequately managed this multibillion dollar

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[4](...continued)
the orders.

> enterprise, the oil and gas industry is not paying all the royalties it rightly owes. . . . The results of individual audits, which have often uncovered large underpayments, suggest that hundreds of millions of dollars due the U.S. Treasury, the States, and Indian tribes are going uncollected every year.

*Id.* at xv, App. 3a.

Congress responded by adopting the royalty reforms in the Federal Oil and Gas Royalty Management Act of 1982, 30 U.S.C. § 1701 *et seq.* (2000) ("FOGRMA"). The legislative history of FOGRMA explains that the oil and gas industry has operated "essentially on an honor system," without sufficient verification of industry reporting, and clarifies that FOGRMA is intended to ensure the prompt and accurate collection of oil and gas royalties. H.R. Rep. No. 97-859, at 15 (1982), *reprinted in* 1982 U.S.C.C.A.N. 4268, 4269; *see also* 30 U.S.C. § 1701 (2000), App. 8a. The House Report estimated that as much as "half a billion dollars is going uncollected annually" and emphasized the importance of this lost revenue to Indian tribes. U.S.C.C.A.N. at 4269-4270.

Unfortunately, the enactment of FOGRMA did not stop the oil and gas companies from finding ways to underpay royalties, and the practice continues to this day. *See, e.g.*, "Wait! There's More Money to Collect," Report of the Project on Government Oversight (August 1996), available at http://www.pogo.org/p/environment/eo-960101-oilroyalties.html (reporting on vast unpaid royalties on oil production since 1985 and describing methods that companies use to reduce royalties, including setting posted prices at artificially low levels; concealing true value of oil through various marketing arrangements; and misreporting

transportation costs and other deductions from the price of oil); *More Public Drilling? Let's Collect Bills First*, USA Today (April 6, 2001), available at http://www.usatoday.com/news/opinion/2001-04-06-nceditf.htm ("industry has shorted the government on oil-royalty payments alone by about $100 million a year" and "similar questions are being raised about gas"); Jim Morris, *Making Them Pay*, US News & World Report, (May 14, 2001), http://www.usnews.com/usnews/biztech/articles/010514/archive_001087.htm (describing various methods of underpaying royalties).

Various False Claims Act lawsuits filed by industry whistleblowers provide further evidence that the oil and gas industry continues to underreport royalties: these lawsuits explain how lessees undervalue gas using a variety of schemes, including by calculating royalties based on sales to affiliates instead of arm's-length transactions; deducting more than the actual costs incurred for transportation and processing services; and undermeasuring and undervaluing gas and natural gas liquids. *See, e.g., U.S. ex rel Harrold E. (Gene) Wright v. AGIP Petroleum Co.*, No. 9:98CV30 (E.D. Tex. filed February 3, 1998), transferred No. 5:03-CV-264 (E.D. Tex.).

Still more evidence is provided by instances in which MMS actually identified these unlawful practices. *See, e.g., Union Texas Petroleum*, 153 IBLA 170, 172 (2000) (failure to perform dual accounting[5]; failure to use accurate volumes and

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[5]Dual accounting, required in Indian leases, means that the lessee must calculate both (1) the value of the unprocessed gas and (2) the combined values of the processed gas and separated liquids after processing (less allowed processing costs), and pay royalties as a percentage of the higher of the two values. 30 C.F.R. §§ 206.155 (1988); *see also* 30 C.F.R. § 206.171 (2005).

Btu measurements; and undervaluation of gas by using contract price instead of maximum lawful price and by taking processing allowance greater than actual cost); *Marathon Oil Co.*, 149 IBLA 287, 292-93 (1999) (failure to dual account); *ARCO*, 131 IBLA 299, 304 (1994) (undervalued production due to miscategorization of oil); *Amoco Production Co.*, 123 IBLA 278, 293 (1992) (repeated royalty underpayments caused by erroneous claims for refunds). Because the oil and gas industry's practice of undervaluing and underreporting royalties dates back about 50 years and continues into the present, it is unavoidable that there are substantial uncollected royalties owing to tribes that would be barred by the six-year statute of limitations.[6]

### B. The Continuing Failure of MMS to Adequately Administer and Enforce Lease Terms has Compounded the Problem of Unpaid Royalties.

In addition, the Interior Department has fallen far short of its duty to "ensure the prompt and proper collection . . . of oil and gas revenues," 30 U.S.C. § 1701(b)(3) (2000), App. 9a.

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[6] Beginning in 2000, companies generally pay royalties on gas from Indian leases based on published index prices, as provided in 30 C.F.R. § 206.172 (2005), intended to minimize opportunities for underreporting and underpayment. The published index prices are, however, based on reports from the oil and gas companies themselves, and do not always reflect the true sale prices. *See Wait! There's More Money to Collect*, Report of the Project on Government Oversight (August 1996) http://www.pogo.org/p/environment/eo-960101-oilroyalties.html (posted prices for oil below fair market value); Edmund L. Andrews, *As Profits Soar, Companies Pay U.S. Less for Gas Rights*, New York Times, January 23, 2006, at A-1 (disparities in prices reported for gas). Moreover, not all tribal leases are subject to this provision, § 206.172(a), and tribes also may request MMS to exclude their leases from this method of valuation, § 206.172(f).

The Linowes Commission found that "[t]he government's royalty recordkeeping for Federal and Indian oil and gas leases is in disarray." Linowes Commission Report at xv, App. 3a. *See also OXY*, 268 F.3d at 1013 (Briscoe, J., dissenting):

> when Congress enacted the FOGRMA it was primarily concerned with (1) lost revenues resulting from poor royalty accounting practices by administrative agencies; (2) substandard auditing and verification procedures; (3) lax security on certain lease sites resulting in theft and fraud; and (4) an inadequate and inflexible array of enforcement tools.

Despite Congressional hearings, remedial legislation, an adverse Inspector General report,[7] and criticisms in the press, the Interior Department's failure to properly administer royalties has continued. Indeed, the Jicarilla Apache Nation was forced to sue the Department to enforce the dual accounting requirement in its leases. *Jicarilla Apache Tribe v. Supron Energy Corp.*, 479 F. Supp. 536, *aff'd in part and rev'd and remanded in part on other grounds*, 782 F.2d 855 (10th Cir. 1986) (*en banc*) (*adopting dissenting opinion at* 728 F.2d 1555 (1984)), *modified*, 793 F. 2d 1171 (10th Cir. 1986), *cert. denied*, 479 U.S. 970 (1986) (Secretary of Interior breached his fiduciary duty to the tribe by failing to administer and enforce the dual accounting and other provisions of the tribe's leases).

By participating in audits of royalty payments, the Jicarilla Apache Nation has discovered many other examples of the Department, through MMS, failing to carry out its royalty

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[7] Final Report on an Audit of the Minerals Management Service Audit Offices, OIG 2003-I-0023 (March 31, 2003), available at http://www.oig.doi.gov/upload/2003i0023.pdf.

management duties. For instance, MMS has failed to account for affiliate sales in verifying the value of gas reported for royalty purposes. *See, e.g., Burlington Resources Oil & Gas Co.*, 151 IBLA 144, 158 (1999) (in calculating major portion prices for gas produced from Indian lands, MMS used a database that did not distinguish between arm's-length and non-arm's-length sales). Because producers can sell gas to affiliated entities at artificially low prices, thus lowering the value of their gas for royalty valuation purposes, and subsequently can have the affiliates resell at a higher price, so that no revenue is lost, *see* Linowes Commission Report at 23, 64, 65, App. 4a - 7a, the arm's-length sale requirement is essential for arriving at a legitimate value for gas.[8]

Other problems arise because the MMS database does not distinguish between Btu values or gas classifications, despite the fact that prices for different Btu values and different gas classifications can vary by wide margins. *See, e.g.*, 30 C.F.R. § 206.154 (1988) (adjustments to be made for gas quality); 30 C.F.R. § 206.173(b) (2005) (providing different values for different Btu ranges). Moreover, when errors in reporting have been discovered through audits, MMS has not gone back to correct its database, so that the undervaluation created by those errors is perpetuated.

MMS also allows oil and gas companies to deduct from their current royalty obligations the amounts they claim they overpaid as royalties in the past, a practice known as taking recoupments. 30 C.F.R. § 218.53 (1988); 30 C.F.R. § 218.53 (2005); *see also Amoco Production Co.*, 173 IBLA at 279. The companies may take recoupments without identifying the

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[8] One of the purposes of the "major portion" provision in Indian leases is to ensure that royalties are paid on values at least equal to those received in comparable arm's-length transactions.

royalties allegedly overpaid, providing ample opportunity to take advantage of the system. Moreover, the current MMS list of recoupments on Indian leases includes recoupments taken for periods going back to 1987, and records balances that are still recoupable for periods going back to 1990. The companies thus are able to go back well beyond six years to make adjustments that reduce their royalty obligations. It would certainly aggravate the royalty underpayment problem if the statute of limitations prevented MMS from reviewing these recoupments and requiring reimbursements when they are incorrectly taken.

As final examples, MMS has routinely permitted companies to claim the maximum permissible amount of transportation and processing costs (which are deducted from the value of gas before royalties are calculated) without verifying that those costs actually were incurred. *See* 30 C.F.R. §§ 206.156(c), 206.157 (1988) (transportation allowances); 30 C.F.R. §§ 206.158(c)(2), 206.159 (1988) (processing allowances). And MMS has failed to enforce against late reporting and late payments, despite the fact that royalties are due the month after the month of production, 30 C.F.R. § 218.50 (1988); 30 C.F.R. § 218.50 (2005), and late payment interest is required under FOGRMA and the MMS regulations, 30 U.S.C. § 1721 (2000); 30 C.F.R. § 218.54 (1988); 30 C.F.R. § 218.54 (2005).

By failing to adequately verify and audit royalty reports and enforce lease terms, MMS has exacerbated the existing problem of royalty underpayments. According to one recent report,

> At a time when energy prices and industry profits are soaring, the federal government collected little more money last year than it did five years ago . . . .The possible losses to

> taxpayers in gas could be even higher than the losses tied to the scandals over oil royalties. For one thing, natural gas production on federal land is worth twice as much as oil. Moreover, the Interior Department has scaled back on full audits, pushed out a couple of its more aggressive auditors and been criticized by its own inspector general for the audits that it did pursue.

Edmund L. Andrews, *As Profits Soar, Companies Pay U.S. Less for Gas Rights*, New York Times, January 23, 2006, at A-1. *See also Making Them Pay* ("For decades, court documents show, producers have set artificially low prices and used other dubious means to underpay by billions of dollars, partly because regulators either weren't mindful or were disinclined to act").[9]

### C. The Audit Process by Its Nature is Retroactive and Lengthy, Often Involving Periods Dating Back More Than Six Years, but It has Confirmed that Substantial Royalties are Owed to Tribes.

The MMS audit process involves the review of records and reports of royalty payments made in the past to determine whether royalties have been correctly calculated; it is thus a

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[9] The Department of the Interior's Office of Inspector General is currently working, together with the General Accounting Office, on yet another report on the scope of underreporting and underpayment by the oil and gas industry of natural gas royalties on public land. Senator Schumer (D-NY) requested the report on January 23, 2006, and it is due to be completed within the next few months. *See* http://www.schumer.senate.gov/SchumerWebsite/pressroom/press_releases/2006/PR19.Gas%20Letter.012306.html.

retroactive process. The audit process is necessary because royalty payments are based on companies' own reports of their sales, 30 C.F.R. pt. 210 (1988); 30 C.F.R. pt. 210 (2005), and it is made even more necessary in light of the companies' long-standing practice of undervaluing and underreporting oil and gas for royalty purposes.

MMS begins an audit by reviewing a few sample months from a few sample leases. If this review reveals errors in reporting, MMS issues a letter to the production company that is the lessee of record, informing the company of the initial finding of discrepancy and allowing the company time to respond. MMS then considers the response and may or may not issue an order calculating the underpayment for the audited months and directing the company to pay any additional royalties due for the remainder of the audit period. *See Union Texas Petroleum*, 153 IBLA at 179; *BHP Petroleum (Americas) Inc.*, 124 IBLA 185, 187-88 (1992) (cases describing the audit process). The MMS order thus already is issued substantially after the audit period in question. Indeed, the MMS audit cases cited in section A above all involved audit periods beginning more than six years before the relevant MMS orders were issued.

In addition, about 15 years ago when the price of natural gas produced from the Jicarilla Apache Reservation dropped and the tribe's revenues fell accordingly, the Jicarilla Apache Nation began reviewing and eventually participating in MMS audits of its leases, *see* FOGRMA § 202, 30 U.S.C. § 1732 (2000). The tribe discovered many of the royalty underpayment schemes described in Section A above, and also discovered that MMS had failed to identify any number of reporting errors, as described in Section B above. Correcting these errors would result in MMS orders that are even more likely than the initial

orders to be issued more than six years from the beginning of the audit period.[10]

Applying the six-year statute of limitations in § 2415(a) to MMS orders to pay additional royalties thus would let oil and gas production companies off the hook for millions of dollars of unpaid royalties, essentially rewarding them for their malfeasance. Moreover, allowing the Tenth Circuit *OXY* decision to stand will have a disproportionate impact on Indian tribes, since many oil- and gas-owning tribes have reservations within the Tenth Circuit. The *OXY* decision has already affected the Jicarilla Apache Nation's ability to negotiate for and collect additional royalties owing to the tribe, for example causing the tribe and MMS to accept discounts in settlements of orders to pay royalties.

Finally, the United States, through the Department of the Interior and MMS, has a trust obligation to ensure that tribes are receiving all the royalties due to them. *See generally Seminole Nation v. United States*, 316 U.S. 286, 296-97 (1942) (seminal case stating that the United States has a "moral obligation of the highest responsibility and trust" to Indian tribes and that the federal government's "conduct . . . in dealings with the Indians, should therefore be judged by the most exacting fiduciary standards"); *Supron*, 728 F.2d at 1563 (Secretary's administration of tribal oil and gas reserves "must not merely meet the minimal requirements of administrative law, but must also pass scrutiny under the more stringent standards demanded of a fiduciary"); *Pawnee v. United States*, 830 F.2d 187, 189-91 (Fed. Cir. 1987), *cert. denied*, 486 U.S. 1032 (1988); *Assiniboine & Sioux Tribes v. Bd. of Oil & Gas Conservation*, 792 F.2d 782, 794 & n.15 (9th Cir. 1986); *see*

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[10]One of the ways these errors have been addressed is through the major portion orders referenced in this brief.

*also* 30 C.F.R. § 206.150(d) (1988); 30 C.F.R. § 206.150(d) (2005) (referring to "the trust responsibilities of the United States with respect to the administration of Indian oil and gas leases"). In fact, the Jicarilla Apache Nation has filed suit against the United States for, *inter alia*, the United States' failure to properly oversee and collect the royalties owed to the tribe. *Jicarilla Apache Nation v. United States*, No. 1:02-cv-00025-FMA (Fed. Cl. filed January 8, 2002). If the Court upholds the D.C. Circuit decision below, liability for underpayment of royalties will be shifted away from the United States and placed squarely on the oil and gas production companies that engaged in various schemes to underpay the royalties in the first instance.

## CONCLUSION

The Court should grant the petition for a writ of certiorari on the question of the statute of limitations.

Respectfully submitted,

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March 13, 2006

## APPENDIX A
## LINOWES COMMISSION REPORT (SELECTED PAGES)

Commission of Fiscal Accountability
of the Nation's Energy Resources
Suite 403
1111 18th St., N.W.
Washington, DC 20036
(202) 653-9051

January 21, 1982

The Honorable James G. Watt
Secretary of the Interior
Washington, D.C. 20240

Dear Mr. Secretary:

I am pleased to transmit to you the report of the Commission on Fiscal Accountability of the Nation's Energy Resources.

During the past six months, the Commission has investigated the serious allegations of massive irregularities in royalty payments due the Federal government, Indian tribes, and States; and the allegations of theft of oil from Federal and Indian lands. From the outset and throughout our deliberations, we have sought and obtained the active participation of all those having particular interests in our findings: State officials, Indian tribes, oil and gas companies, United States Geological Survey and others within the Department of the Interior, General Accounting Office, and committees of Congress, among others.

In its work, the Commission has maintained a position of independence and objectivity, giving full and balanced

consideration to all points of view. We believe our findings give a comprehensive and fair analysis of the conditions and relationships that now prevail within and among the institutions involved in royalty management. It is the unanimous judgment of the Commission that if the accompanying recommendations are adopted, a major step will have been taken to bring full and proper accountability to the management of Federal royalties.

Participation in the work of the Commission has been a challenging opportunity to serve our Nation, and to join in the President's attack on fraud, waste and inefficiency in the Federal government. We appreciate having this privilege.

Respectfully submitted,

David F. Linowes
Chairman

# SUMMARY

Management of royalties for the Nation's energy resources has been a failure for more than 20 years. Because the Federal government has not adequately managed this multibillion dollar enterprise, the oil and gas industry is not paying all the royalties it rightly owes.

The government's royalty recordkeeping for Federal and Indian oil and gas leases is in disarray. For this reason, the exact amount of underpayment is unknown. The results of individual audits, which have often uncovered large underpayments, suggest that hundreds of millions of dollars due the U.S. Treasury, the States, and Indian tribes are going uncollected every year.

In addition, oil thefts are occurring on Federal and Indian leases. The extent of theft and the amount of royalty losses from theft are unknown, but it is well-documented that security at many Federal and Indian lease sites is lax and is an open invitation to theft.

The Nation can no longer afford mismanagement of royalties for its energy resources. The stakes are too high. With the rapid escalation of energy prices oil and gas royalties have risen from less than $500 million in 1971 to more than $4 billion in 1981.

The government's royalty management system needs a thorough overhaul. This report of the Commission on Fiscal Accountability of the Nation's Energy Resources details 60 specific recommendations (listed in Chapter Nine of the report) for revising and rebuilding the system. Underlying these recommendations are some fundamental conclusions

the Commission reached in the course of its intensive inquiry:

. . .

*23*

undervaluation of natural gas was the largest factor in royalty underpayments. Because of the growing importance of natural gas as a source of royalty income, proper valuation of gas is especially important. In 1980, gas accounted for 56 percent of all energy mineral royalties on Federal and Indian lands. According to Interior Department projections, it will contribute approximately 75 percent by 1990.

Federal and Indian royalties on oil and gas are based on "fair market value," which cannot be less than the sales price and may be more. The complexities of establishing this value leave a wide latitude for differing interpretations. The USGS routinely accepts oil and gas companies' valuation of the product on which royalties are paid.

A major problem in setting fair market value for oil and gas is that large, vertically integrated companies in effect sell to themselves. These companies produce crude oil or natural gas, transport it, process it, and sell it, often to the final customer. The USGS rules require that integrated companies calculate royalties on crude oil or gas sold within the company on the basis of "market value," equal at least to what an independent buyer would pay.

Government price controls and longterm contracts for natural gas add complications. Oil price controls were lifted by President Reagan in January 1981, but natural gas price controls for interstate sales still exist and are scheduled to last until 1985. The controlled prices differ greatly according to the

date production began, with old prices far below current prices. Likewise, old prices are frozen into some
longterm gas contracts even where price controls do not apply. There are currently 27 different controlled prices for interstate sales of natural gas, a situation which allows many differences in interpretation of value

. . .

*64*

PROBLEM: DETERMINING THE VALUE OF PRODUCTION

Most major audits conducted so far have found under-valuation of gas produced from Federal and Indian leases to be the biggest cause of royalty underpayments. Eleven major natural gas royalty audits were conducted by the Department of the Interior's Office of the Inspector General (formerly the Office of Audit and Investigation) from 1977 through 1981. Ten of the audits showed underpayments, of which nine were mainly due to undervaluation of the product.[11] (One audit showed an overpayment; the underpayments ranged from $684 to more than $10 million.) Royalties for natural gas already account for 56 percent of total Federal and Indian oil and gas royalties; by 1990, they are expected to be approximately 75 percent of the total. Thus, it is especially important to give attention to valuation of natural gas.

For valuation of oil and gas, as for reporting of production volumes, sales, and royalties, USGS usually accepts industry

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[11] In one of the nine cases the assessment of additional royalties was reversed on appeal by the Interior Department's Office of Hearing and Appeals. Three are currently on appeal.

date without verification. The Mineral Leasing Act of 1920 and the Indian leasing Act of 1927 specify that royalties shall be based on the "value of the production." The Outer Continental Shelf Act says that "fair market value" shall be received for the "lands leased and the rights conveyed."

Under these laws, USGS regulations base royalties on "estimated reasonable value," which "in the absence of good reason to the contrary," is the "value computed on the basis of the highest price...paid



or offered at the time of production in a fair and open market..." The fair market value, according to these rules, cannot be less than actual sales prices and may be more. In practice, however, the Geological Survey accepts the value of the product set by the industry—which is almost always the sales price—and relies on audits or lease analysis to correct any undervaluation.

Valuation problems occur especially with internal sales in vertically integrated companies, with longterm contracts, and with price-controlled products. Gas is especially subject to these problems since it is commonly sold by longterm contract, and some of it is price controlled. Other difficulties in valuation have to do with deductions allowed (from value of the product before the royalty is computed) for the costs of transporting oil or gas to a point of sale off the lease, and for the costs of processing natural gas (removing liquids).

Some examples of underpayment of royalties due to undervaluation are:

- A vertically integrated company using in its own refineries gas it had produced was allowed by USGS to use longterm contract prices, rather than higher current market prices, as a basis for royalties. An audit by the Interior Department's Office of Audit and Investigation showed underpayment for a 10-year period of $2.2 million. The underpayment amounted to 31 percent of royalties actually paid ($6.9 million).

- A review of offshore leases by the Office of the Audit and Investigation showed that offshore

...

# APPENDIX B
# RELEVANT STATUTORY AND REGULATORY PROVISIONS

## 1. Federal Oil and Gas Royalty Management Act of 1982

### 30 U.S.C. § 1701. Congressional statement of findings and purposes

**(a)** Congress finds that--

**(1)** the Secretary of the Interior should enforce effectively and uniformly existing regulations under the mineral leasing laws providing for the inspection of production activities on lease sites on Federal and Indian lands;

**(2)** the system of accounting with respect to royalties and other payments due and owing on oil and gas produced from such lease sites is archaic and inadequate;

**(3)** it is essential that the Secretary initiate procedures to improve methods of accounting for such royalties and payments and to provide for routine inspection of activities related to the production of oil and gas on such lease sites; and

**(4)** the Secretary should aggressively carry out his trust responsibility in the administration of Indian oil and gas.

**(b)** It is the purpose of this chapter--

**(1)** to clarify, reaffirm, expand, and define the responsibilities and obligations of lessees, operators, and other persons

involved in transportation or sale of oil and gas from the Federal and Indian lands and the Outer Continental Shelf;

**(2)** to clarify, reaffirm, expand, and define the authorities and responsibilities of the Secretary of the Interior to implement and maintain a royalty management system for oil and gas leases on Federal lands, Indian lands, and the Outer Continental Shelf;

**(3)** to require the development of enforcement practices that ensure the prompt and proper collection and disbursement of oil and gas revenues owed to the United States and Indian lessors and those inuring to the benefit of States;

**(4)** to fulfill the trust responsibility of the United States for the administration of Indian oil and gas resources; and

**(5)** to effectively utilize the capabilities of the States and Indian tribes in developing and maintaining an efficient and effective Federal royalty management system.

(Pub.L. 97-451, § 2, Jan. 12, 1983, 96 Stat. 2448.)

. . .

INDIAN LANDS

Pub.L. 104-185, § 9, Aug. 13, 1996, 110 Stat. 1717, provided that: "The amendments made by this Act [see Short Title of 1996 Amendments note set out under this section] shall not apply with respect to Indian lands, and the provisions of the Federal Oil and Gas Royalty Management Act of 1982 [this chapter] as in effect on the day before the date of enactment of

this Act [Aug. 13, 1996] shall continue to apply after such date with respect to Indian lands."

. . .

## 2. 30 C.F.R. Part 218: Collection of Royalties, Rentals, Bonuses, And Other Monies Due The Federal Government

### § 218.50 Timing of Payment

**(a)** Royalty payments are due at the end of the month following the month during which the oil and gas is produced and sold except when the last day of the month falls on a weekend or holiday. In such cases, payments are due on the first business day of the succeeding month. Rental payments are due as specified by the lease terms.

**(b)** Payments made on a Bill for Collection (Form DI-104b) are due as specified by the Bill. Bills for Collection will be issued and payable as final collection actions.

**(c)** All payments to MMS are due as specified and are not deferred or suspended by reason of an appeal having been filed unless such deferral or suspension is approved in writing by an authorized MMS official.

### § 218.53 Recoupment of overpayments on Indian mineral leases

**(a)** Whenever an overpayment is made under an Indian oil and gas lease, a payor may recoup the overpayment through a recoupment on Form MMS-2014 against the current month's royalties or other revenues owed on the same lease. However, for any month a payor may not recoup more than 50 percent of the royalties or other revenues owed in that month under an individual allotted lease or more than 100 percent of the

royalties or other revenues owed in that month under a tribal lease.

**(b)** With written permission authorized by tribal statute or resolution, a payor may recoup an overpayment against royalties or other revenues owed in that month under other leases for which that tribe is the lessor. A copy of the tribe's written permission must be furnished to MMS pursuant to instructions for reporting recoupments in the MMS "Oil and Gas Payor Handbook." See 30 CFR 210.53. Recouping overpayments on one allotted lease is specifically prohibited.

**(c)** Overpayments subject to recoupment under this section include all payments made in excess of the required payment for royalty, rental, bonus, or other amounts owed as specified by statute, regulation, order, or terms of an Indian mineral lease.

**(d)** The MMS Director or his/her designee may order any payor to not recoup any amount for such reasonable period of time as may be necessary for MMS to review the nature and amount of any claimed overpayment.

**§ 218.54 Late Payments**

**(a)** An interest charge shall be assessed on unpaid and underpaid amounts from the date the amounts are due.

**(b)** The interest charge on late payments shall be at the underpayment rate established by the Internal Revenue Code, 26 U.S.C. 6621(a)(2) (Supp. 1987)

**(c)** Interest will be charged only on the amount of the payment not received. Interest will be charged only for the number of days the payment is late.

**(d)** A portion of the interest collected will be paid to a State where the State shares in mineral revenues from Federal leases.

**(e)** An overpayment on a lease or leases may be offset against an underpayment on a different lease or leases to determine a net underpayment on which interest is due pursuant to conditions specified in §218.42.

No. 05-669

FILED
JUN 13 2006
OFFICE OF THE CLERK
SUPREME COURT, U.S.

IN THE

# Supreme Court of the United States

BP AMERICA PRODUCTION COMPANY AND
ATLANTIC RICHFIELD COMPANY,
*Petitioners,*

v.

REJANE BURTON,
ACTING ASSISTANT SECRETARY OF THE INTERIOR
FOR LAND AND MINERALS MANAGEMENT, *et al.*,
*Respondents.*

**On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit**

## JOINT APPENDIX

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PETITION FOR A WRIT OF CERTIORARI FILED – NOVEMBER 22, 2005
PETITION FOR A WRIT OF CERTIORARI GRANTED – APRIL 17, 2006

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**IN THE**
**UNITED STATES COURT OF APPEALS**
**FOR THE DISTRICT OF COLUMBIA CIRCUIT**

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Docket No. 04-5006

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AMOCO PRODUCTION COMPANY,
PLAINTIFF - APPELLANT,

V.

REBECCA W. WATSON, *et al.*,
DEFENDANTS - APPELLEES.

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**RELEVANT DOCKET ENTRIES**

| DATE | PROCEEDINGS |
|---|---|
| 1/19/04 | CIVIL-US CASE docketed. Notice of Appeal filed by Appellant Amoco Prodn Co. [798152-1] (sha) [04-5006] |
| | * * * * * |
| 2/2/04 | CLERK'S ORDER filed [800434] to consolidate cases |
| | * * * * * |
| 3/3/04 | INITIAL SUBMISSIONS filed by Appellants Amoco Prodn Co in 04-5006, and Vastar Resrc Inc., and Atl Richfield Co. in 04-5007 [807509]: docketing statement; certificate of counsel; statement of issues; the lower court decisions; deferred appendix notice (Deferred Appendix needed = y ). [04-5006, 04-5007] (jth) [04-5006 04-5007] |

| DATE | PROCEEDINGS |
|---|---|
| 3/3/04 | INITIAL SUBMISSIONS filed by Federal Appellees DOI, et al., in 04-5006, 04-5007 [807518-1]: certificate of counsel. [04-5006, 04-5007] (jth) [04-5006 04-5007] |
| | * * * * * |
| 6/15/04 | CLERK'S ORDER filed [828510] to schedule oral argument |
| | [828510-1] before Judge Initials: DBS JGR SFW on 2/14/05 at 9:30 AM. [Entry Date: 6/15/04] [04-5006, 04-5007] (cwc) [04-5006 04-5007] |
| 7/14/04 | BRIEF filed by Appellants Amoco Production Co. in 04-5006, and Appellants Vastar Resources, Inc., Atlantic Richfield Company in 04-5007 [836821-1]. (Copies: 8). Certificate of mail service dated 7/14/04. [04-5006, 04-5007] (jth) [04-5006 04-5007] |
| 7/28/04 | BRIEF filed by Amicus Curiae for Appellant Burlington Resrc Inc in 04-5006 and 04-5007 [839218-1]. Copies: 7. Certificate of service date 7/28/04. [04-5006, 04-5007] (mam) [04-5006 4-5007] |
| | * * * * * |
| 10/4/04 | BRIEF filed by Appellee Gale A. Norton in 04-5006, Appellee DOI in 04-5006, Appellee Rebecca W. Watson in 04-5006, Appellee Gale A. Norton in 04-5007, Appellee DOI in 04-5007, Appellee Rebecca W. Watson in 04-5007 [853652-1]. Copies: 7. Certificate of service date 10/4/04. [04-5006, 04-5007] (lme) [04-5006 04-5007] |

| DATE | PROCEEDINGS |
|---|---|
| 10/13/04 | ERRATA TO INITIAL BRIEF FOR THE APPELLEES FILED ON 10/4/04 [858322-1] of (certificate of service dated 10/12/04, by mail) [853652-1] in 04-5006, 04-5007 filed by Appellees Gale A. Norton, DOI, Rebecca W. Watson in 04-5006, 04-5007. [04-5006, 04-5007] (lvs) [04-5006 04-5007] |
| | * * * * * |
| 10/19/04 | JOINT BRIEF w/ATTACHED ADDENDUM filed by Amicus Curiae for Appellees St CO, So Ute Indian Tribe, Assiniboine Sioux, Jicarilla Apache, St NM, CA St Controller in 04-5006, 04-5007 [858332-1]. 7 COPIES OF EACH. Certificate of service date 10/19/04, by mail). [04-5006, 04-5007] (lvs) [04-5006 04-5007] |
| 11/19/04 | JOINT REPLY BRIEF filed by Appellant Amoco Prodn Co in 04-5006, Appellants Vastar Resrc Inc, Atl Richfield Co in 04-5007 [864730-1]. Copies: 7. Certificate of service date 11/19/04, by mail. [04-5006, 04-5007] (lvs) [04-5006 04-5007] |
| 12/3/04 | JOINT APPENDIX [VOLUMES I & II] filed by Appellant Amoco Prodn Co in 04-5006, Appellants Vastar Resrc Inc, Atl Richfield Co in 04-5007 [864741-1]. Copies: 10. Certificate of service date 12/3/04. [04-5006, 04-5007] (lvs) [04-5006 04-5007] |
| 12/6/04 | SUPPLEMENTAL APPENDIX lodged by Appellants [864530-1]. Copies: 10. Certificate of service date 12/6/04. [04-5006, 04-5007] (lej) [04-5006 04-5007] |
| | * * * * * |

| DATE | PROCEEDINGS |
|---|---|
| 12/9/04 | FINAL BRIEF filed by Appellee Gale A. Norton, Appellee DOI, Appellee Rebecca W. Watson in 04-5006, 04-5007 [866784-1]. Copies: 15. Certificate of service date 12/9/04. [04-5006, 04-5007] (wmw) [04-5006 04-5007] |
| 12/10/04 | FINAL BRIEF filed by Appellant Amoco Prodn Co in 04-5006, Appellant Vastar Resrc Inc, Appellant Atl Richfied Co in 04-5007 [866767-1]. Copies: 15. Certificate of service date 12/10/04. [04-5006, 04-5007] (wmw) [04-5006 04-5007] |
| 12/10/04 | FINAL BRIEF filed by Amicus Curiae for Appellant Burlington Resrc Inc in 04-5006, 04-5007 [866808-1]. Copies: 15. Certificate of service date 12/10/04. [04-5006, 04-5007] (wmw) [04-5006 04-5007] |

**IN THE**
**UNITED STATES DISTRICT COURT**
**FOR THE DISTRICT OF COLUMBIA**

---

Case No. 1:00-cv-02933-WBB

---

AMOCO PRODUCTION COMPANY,

PLAINTIFF,

v.

SYLVIA V. BACA, *et al.*,

DEFENDANTS.

---

**RELEVANT DOCKET ENTRIES**

| DATE | NO. | PROCEEDINGS |
|---|---|---|
| 12/08/00 | 1 | COMPLAINT filed by Plaintiff AMOCO PRODUCTION CO; Exhibits (3). (jeb) (Entered: 12/14/2000) |
| | | * * * * * |
| 03/06/01 | 11 | ANSWER TO COMPLAINT [1-1] by federal defendants SYLVIA V. BACA, BRUCE BABBITT, and DOI. (ag) (Entered: 03/07/2001) |
| | | * * * * * |
| 08/20/01 | 15 | MOTION filed by plaintiff AMOCO PRODUCTION CO for summary judgment (cas) (Entered: 08/29/2001) |
| | | * * * * * |

| DATE | NO. | PROCEEDINGS |
|---|---|---|
| 09/24/01 | 16 | ADMINISTRATIVE RECORD by federal defendant SYLVIA V. BACA, federal defendant BRUCE BABBITT, federal defendant DOI; five volumes (nmr) (Entered: 09/25/2001) |
| | | * * * * * |
| 11/20/01 | 21 | RESPONSE by plaintiff AMOCO PRODUCTION CO in opposition to Defendants' Consolidated Motion for Summary Judgment; Exhibits (7) (nmr) (Entered: 11/20/2001) |
| 11/20/01 | 22 | REPLY by plaintiff AMOCO PRODUCTION CO to response in opposition to motion for summary judgment [15-1] by AMOCO PRODUCTION CO; Exhibits (7) (nmr) (Entered: 11/20/2001) |
| | | * * * * * |
| 12/20/01 | 25 | REPLY by federal defendant in support of federal defendant's Consolidated Motion for Summary Judgment. (nmr) (Entered: 12/21/2001) |
| | | * * * * * |
| 01/15/02 | 28 | SURREPLY by plaintiff AMOCO PRODUCTION CO to motion for summary judgment [15-1] by AMOCO PRODUCTION CO (nmr) (Entered: 01/16/2002) |
| 02/11/02 | 29 | NOTICE OF SUPPLEMENTAL AUTHORITY by plaintiff AMOCO PRODUCTION CO (td) (Entered: 02/13/2002) |
| | | * * * * * |

| DATE | NO. | PROCEEDINGS |
|---|---|---|
| 02/21/02 | 32 | MOTION (unopposed) filed by plaintiff AMOCO PRODUCTION CO for leave to file joint reply to defendant's response to plaintiffs' notice of supplemental authority; EXHIBIT (Joint Reply) (td) (Entered: 02/26/2002) |
| 02/21/02 | 40 | RESPONSE by federal defendant SYLVIA V. BACA, federal defendant BRUCE BABBITT, federal defendant DOI to notice of supplemental authority [29-1]. by AMOCO PRODUCTION CO (td) (Entered: 09/10/2002) |
| 03/05/02 | 33 | ORDER by Judge William B. Bryant: granting motion for leave to file joint reply to defendants' response to plaintiffs' notice of supplemental authority [32-1] by AMOCO PRODUCTION CO (N) (dam) (Entered: 03/05/2002) |
| 03/13/02 | 34 | MOTION filed by movant SOUTHERN UTE for leave to file brief of amicus curiae in support of defendants' motion for summary judgment; EXHIBIT (Amicus) (td) (Entered: 03/18/2002) |
| 03/18/02 | 35 | RESPONSE by plaintiff AMOCO PRODUCTION CO in opposition to motion for leave to file brief of amicus curiae in support of defendants' motion for summary judgment [34-1] by SOUTHERN UTE. (jf) (Entered: 03/20/2002) |
| 03/21/02 | 36 | REPLY (joint) by plaintiff AMOCO PRODUCTION CO to defendants' response to plaintiffs' notice of supplemental authority [29-1] by AMOCO PRODUCTION CO. (td) (Entered: 03/27/2002) |

| DATE | NO. | PROCEEDINGS |
|---|---|---|
| 04/26/02 | 37 | MOTION (unopposed) filed by plaintiff AMOCO PRODUCTION CO for leave to file joint reply to brief of amicus curiae; EXHIBIT (joint reply) (td) (Entered: 05/01/2002) |
| 05/03/02 | 38 | ORDER by Judge William B. Bryant; granting motion for leave to file joint reply to brief of amicus curiae [37-1] by AMOCO PRODUCTION CO (N) (dam) (Entered: 05/03/2002) |
| 05/03/02 | 39 | REPLY by plaintiff AMOCO PRODUCTION CO to amicus curiae brief of Southern Ute Indian Tribe. (td) (Entered: 09/10/2002) |
| 11/17/03 | 41 | ORDER denying [15] Motion for Summary Judgment. Signed by Judge William B. Bryant on 11/14/03. (lcwbbl,) (Entered: 11/17/2003) |
| 11/17/03 | 42 | MEMORANDUM for the reasons set forth herein, in an accompanying Order, the Court will deny the Plaintiffs' Motions for Summary Judgment and grant the Defendants' Motion for Summary Judgment. Signed by Judge William B. Bryant on 11/14/03. (lcwbbl,) (Entered: 11/17/2003) |
| 01/07/04 | 43 | NOTICE OF APPEAL as to 41 Order on Motion for Summary Judgment, 42 Memorandum & Opinion, by AMOCO PRODUCTION COMPANY. Filing fee $ 255, receipt number 120308. (cp,) (Entered: 01/08/2004) |

| DATE | NO. | PROCEEDINGS |
|---|---|---|
| 01/08/04 | | Transmission of Notice of Appeal and Docket Sheet to US Court of Appeals re 43 Notice of Appeal (cp,) (Entered: 01/08/2004) |
| 1/21/04 | 44 | USCA case number 04-5006 for 43 Notice of Appeal filed by AMOCO PRODUCTION CO. (cp,) (Entered: 01/23/2004) |
| 09/14/05 | 45 | USCA JUDGMENT (certified copy) as to 43 Notice of Appeal filed by AMOCO PRODUCTION CO; It is hereby ordered and adjudged that the judgment of the District Court appealed from in these causes is hereby affirmed, in accordance with the opinion of the court; USCA#04-5006 (jsc) (Entered: 09/14/2005) |

[unintelligible] UNITED STATES Office Santa Fe
DEPARTMENT OF THE INTERIOR Serial 079012
BUREAU OF LAND MANAGEMENT

[UNINTELLIGIBLE]

NONCOMPETITIVE
**LEASE OF OIL AND GAS LANDS**
**UNDER THE ACT OF**
**FEBRUARY 25, 1920, AS AMENDED**

THIS INDENTURE OF LEASE, entered into, in triplicate, as of the _____ day of _____ by and between the UNITED STATES OF AMERICA, through the Bureau of Land Management, party of the first part, and

Daniel A. Macpherson, Jr.,
1113 West Lead,
Albuquerque, New Mexico,

party of the second part, hereinafter called the lessee, under, pursuant, and subject to the terms and provisions of the act of February 25, 1920, 41 Stat. 437, as amended, hereinafter referred to as the act, and to all reasonable regulations of the Secretary of the Interior now or hereafter in force when not inconsistent with any express and specific provisions herein, which are made a part hereof, WITNESSETH:

SECTION 1. Rights of Lessee.—That the lessor, in consideration of rents and royalties to be paid, and the conditions and covenants to be observed as herein set forth, does hereby grant and lease to the lessee the exclusive right and privilege to drill for, mine, extract, remove, and dispose of all the oil and gas deposits except helium gas in or under the following-described tracts of land situated in ~~the field~~:

T. 30 M., B. 6 W., M.M.P.M., New Mexico,

Sec. 4, All;
Sec. 9, All;

Sec. 17, All;
Sec. 18, All;

x
x
x
x
x
x
x
x

containing 2559.84 acres, more or less, together with the right to construct and maintain thereupon all works, buildings, plants, waterways, roads, telegraph or telephone lines, pipe lines, reservoirs, tanks, pumping stations, or other structures necessary to the full enjoyment thereof, for a period of 5 years, and so long thereafter as oil or gas is produced in paying quantities: subject to any unit agreement heretofore or hereafter approved by the Secretary of the Interior, the provisions of said agreement to govern the lands subject thereto where inconsistencies with the terms of this lease occur.

SEC. 2. In consideration of the foregoing, the lessee hereby agrees:

(a) Bonds.—(1) To maintain any bond furnished by the lessee as a condition for the issuance of this lease. (2) If the lease is issued noncompetitively, to furnish a bond in a sum double the amount of the $1 per acre annual rental, but not less than $1,000 nor more than $5,000, upon the inclusion of any part of the leased land within the geologic structure of a producing oil or gas field. (3) To furnish prior to beginning of drilling operations and maintain at all times thereafter as required by the lessor a bond in the penal sum of $5,000 with approved corporate surety, or with deposit of United States bonds as surety therefor, conditioned upon compliance with the terms of this lease, unless a bond in that

amount is already being maintained or unless such a bond furnished by an approved operator of the lease is accepted.

Until a general lease bond is filed a noncompetitive lessee will be required to furnish and maintain a bond in the penal sum of not less than $1,000 in those cases in which a bond is required by law for the protection of the owners of surface rights. In all other cases where a bond is not otherwise required, a $1,000 bond must be filed for compliance with the lease obligations not less than 90 days before the due date of the next unpaid annual rental, but this requirement may be successively dispensed with by payment of each successive annual rental not less than 90 days prior to its due date.

(b) Cooperative or unit plan.—Within 30 days of demand, or if the land is within an approved unit plan, in the event such a plan is terminated prior to the expiration of this lease, within 30 days of demand made thereafter, to subscribe to and to operate under such reasonable cooperative or unit plan for the development and operation of the area, field, or pool, or part thereof, embracing the lands included herein as the Secretary of the Interior may determine to be practicable and necessary or advisable, which plan shall adequately protect the rights of all parties in interest, including the United States.

(c) Wells.—(1) To drill and produce all wells necessary to protect the leased land from drainage by wells on lands not the property of the lessor or lands of the United States leased at a lower royalty rate, or in lieu of any part of such drilling and production, with the consent of the Director of the Geological Survey, to compensate the lessor in full each month for the estimated loss of royalty through drainage in the amount determined under instructions of said Secretary; (2) at the election of the lessee, to drill and produce other wells in conformity with any system of well spacing or production allotments affecting the field or area in which the leased lands are situated, which is authorized and

sanctioned by applicable law or by the Secretary of the Interior; and (3) promptly after due notice in writing to drill and produce such other wells as the Secretary of the Interior may require to insure diligence in the development and operation of the property.

(d) Rentals and royalties.—(1) To pay the rentals and royalties set out in the rental and royalty schedule attached hereto and made a part hereof.

(2) It is expressly agreed that the Secretary of the Interior may establish reasonable minimum values for purposes of computing royalty on any or all oil, gas, natural gasoline, and other products obtained from gas; due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters and, whenever appropriate, after notice and opportunity to be heard.

(3) When paid in value, such royalties on production shall be due and payable monthly on the last day of the calendar month next following the calendar month in which produced. When paid in amount of production, such royalty products shall be delivered in merchantable condition on the premises where produced without cost to lessor, unless otherwise agreed to by the parties hereto, at such times and in such tanks provided by the lessee as reasonably may be required by the lessor, but in no case shall the lessee be required to hold such royalty oil or other products in storage beyond the last day of the calendar month next following the calendar month in which produced. The lessee shall not be responsible or held liable for the loss or destruction of royalty oil or other products in storage from causes over which he has no control.

(4) Royalties shall be subject to reduction on the entire leasehold or on any portion thereof segregated for royalty purposes if the Secretary of the Interior finds that the lease

cannot be successfully operated upon the royalties fixed herein, or that such action will encourage the greatest ultimate recovery of oil or gas or promote conservation.

(e) Contracts for disposal of products.—Not to sell or otherwise dispose of oil, gas, natural gasoline, and other products of the lease except in accordance with a contract or other arrangement first approved by the Director of the Geological Survey or his representative, such approval to be subject to review by the Secretary of the Interior but to be effective unless and until revoked by the Secretary or the approving officer, and to file with such officer all contracts or full information as to other arrangements for such sales.

(f) Statements, plats, and reports.—At such times and in such form as the lessor may prescribe, to furnish detailed statements showing the amounts and quality of all products removed and sold from the lease, the proceeds therefrom, and the amounts used for production purposes or unavoidably lost; a plat showing development work and improvements on the leased lands and a report with respect to stockholders, investment, depreciation, and costs.

(g) Well records.—To keep a daily drilling record, a log, and complete information on all well surveys and tests in form acceptable to or prescribed by the lessor of all wells drilled on the leased lands, and an acceptable record of all subsurface investigations affecting said lands, and to furnish them, or copies thereof to the lessor when required.

(h) Inspection.—To keep open at all reasonable times for the inspection of any duly authorized officer of the Department, the leased premises and all wells, improvements, machinery, and fixtures thereon and all books, accounts, maps, and records relative to operations and surveys or investigations on the leased lands or under the lease.

(i) Payments.—Unless otherwise directed by the Secretary of the Interior, to make rental, royalty, or other payments to the lessor, to the order of the Treasurer of the

United States, such payments to be tendered to the manager of the district land office in the district in which the lands are located or to the Director of the Bureau of Land Management if there is no district land office in the State in which the lands are located.

(j) Diligence—Prevention of waste—Health and safety of workmen.—To exercise reasonable diligence in drilling and producing the wells herein provided for unless consent to suspend operations temporarily is granted by the lessor; to carry on all operations in accordance with approved methods and practice as provided in the operating regulations, having due regard for the prevention of waste of oil or gas or damage to deposits or formations containing oil, gas, or water or to coal measures or other mineral deposits, for conservation of gas energy, for the preservation and conservation of the property for future productive operations, and for the health and safety of workmen and employees; to plug properly and effectively all wells before abandoning the same; to carry out at expense of the lessee all reasonable orders of the lessor relative to the matters in this paragraph, and that on failure of the lessee so to do the lessor shall have the right to enter on the property and to accomplish the purpose of such orders at the lessee's cost: Provided, that the lessee shall not be held responsible for delays or casualties occasioned by causes beyond lessee's control.

(k) Taxes and wages—Freedom of purchase.—To pay when due, all taxes lawfully assessed and levied under the laws of the State or the United States upon improvements, oil, and gas produced from the lands hereunder, or other rights, property, or assets of the lessee; to accord all workmen and employees complete freedom of purchase, and to pay all wages due workmen and employees at least twice each month in the lawful money of the United States.

(l) Nondiscrimination.—Not to discriminate against any employee or applicant for employment because of race,

creed, color, or national origin, and to require an identical provision to be included in all subcontracts.

(m) Assignment of oil and gas lease or interest therein.—To file within 90 days from the date of final execution any instrument of transfer made of this lease, or any interest therein, including assignments of record title, working or royalty interests, operating agreements and subleases for approval, such instrument to take effect upon its final approval by the Director, Bureau of Land Management, as of the first day of the lease month following the date of filing in the proper land office.

(n) Pipe lines to purchase or convey at reasonable rates and without discrimination.—If owner, or operator, or owner of a controlling interest in any pipe line or of any company operating the same which may be operated accessible to the oil or gas derived from lands under this lease, to accept and convey and, if a purchaser of such products, to purchase at reasonable rates and without discrimination the oil or gas of the Government or of any citizen or company not the owner of any pipe line, operating a lease or purchasing or selling oil, gas, natural gasoline, or other products under the provisions of the act.

(o) Reserved deposits.—To comply with all statutory requirements and regulations thereunder, if the lands embraced herein have been or shall hereafter be disposed of under the laws reserving to the United States the deposits of oil and gas therein, subject to such conditions as are or may hereafter be provided by the laws reserving such oil or gas.

(p) Reserved or segregated lands.—If any of the land included in this lease is embraced in a reservation or segregated for any particular purpose, to conduct operations thereunder in conformity with such requirements as may be made by the Director, Bureau of Land Management, for the protection and use of the land for the purpose for which it

was reserved or segregated, so far as may be consistent with the use of the land for the purpose of this lease, which latter shall be regarded as the dominant use unless otherwise provided herein or separately stipulated.

(q) Overriding royalties.—To limit the obligation to pay overriding royalties or payments out of production in excess of 5 percent to periods during which the average production per well per day is more than 15 barrels on an entire leasehold or any part of the area thereof or any zone segregated for the computation of royalties.

(r) Deliver premises in cases of forfeiture.—To deliver up the premises leased, with all permanent improvements thereon, in good order and condition in case of forfeiture of this lease; but this shall not be construed to prevent the removal, alteration, or renewal of equipment and improvements in the ordinary course of operations.

SEC. 3. The lessor expressly reserves:

(a) Rights reserved—Easements and rights-of-way.—The right to permit for joint or several use easements or rights-of-way, including easements in tunnels upon, through, or in the lands leased, occupied, or used as may be necessary or appropriate to the working of the same or of other lands containing the deposits described in the act, and the treatment and shipment of products thereof by or under authority of the Government, its lessees or permittees, and for other public purposes.

(b) Disposition of surface.—The right to lease, sell, or otherwise dispose of the surface of any of the lands embraced within this lease which are owned by the United States under existing law or laws hereafter enacted, insofar as said surface is not necessary for the use of the lessee in the extraction and removal of the oil and gas therein.

(c) Monopoly and fair prices.—Full power and authority to promulgate and enforce all orders necessary to insure the sale of the production of the leased lands to the United

States and to the public at reasonable prices, to protect the interest of the United States, to prevent monopoly, and to safeguard the public welfare.

(d) Helium.—Pursuant to section 1 of the act, and section 1 of the act of March 3, 1927 (44 Stat. 1387), as amended, the ownership and the right to extract helium from all gas produced under this lease, subject to such rules and regulations as shall be prescribed by the Secretary of the Interior. In case the lessor elects to take the helium the lessee shall deliver all gas containing same, or portion thereof desired, to the lessor at any point on the leased premises in the manner required by the lessor, for the extraction of the helium in such plant or reduction works for that purpose as the lessor may provide, whereupon the residue shall be returned to the lessee with no substantial delay in the delivery of gas produced from the well to the purchaser thereof. The lessee shall not suffer a diminution of value of the gas from which the helium has been extracted, or loss otherwise, for which he is not reasonably compensated, save for the value of the helium extracted. The lessor further reserves the right to erect, maintain, and operate any and all reduction works and other equipment necessary for the extraction of helium on the premises leased.

(e) Taking of royalties.—All rights pursuant to section 36 of the act, to take royalties in amount or in value of production.

(f) Casing.—All rights pursuant to section 40 of the act to purchase casing and lease or operate valuable water wells.

(g) Fissionable materials.—Pursuant to the provisions of the act of August 1, 1946 (Public Law 585, 79th Congress) all uranium, thorium, or other material which has been or may hereafter be determined to be peculiarly essential to the production of fissionable materials, whether or not of commercial value, together with the right of the United

States through its authorized agents or representatives at any time to enter upon the land and prospect for, mine and remove the same, making just compensation for any damage or injury occasioned thereby.

SEC. 4. Drilling and producing restrictions.—It is covenanted and agreed that the rate of prospecting and developing and the quantity and rate of production from the lands covered by this lease shall be subject to control in the public interest by the Secretary of the Interior, and in the exercise of his judgment the Secretary may take into consideration, among other things, Federal laws, State laws, and regulations issued thereunder, or lawful agreements among operators regulating either drilling or production, or both. After unitization, the Secretary of the Interior, or any person, committee, or State or Federal officer or agency so authorized in the unit plan, may alter or modify from time to time, the rate of prospecting and development and the quantity and rate of production from the lands covered by this lease.

SEC. 5. Surrender and termination of lease.—The lessee may surrender this lease or any legal subdivision thereof by filing in the proper land office a written relinquishment, in triplicate, which shall be effective as of the date of filing subject to the continued obligation of the lessee and his surety to make payment of all accrued rentals and royalties and to place all wells on the land to be relinquished in condition for suspension or abandonment in accordance with the regulations and the terms of the lease, to be accompanied by a statement that all wages and moneys due and payable to the workmen employed on the land relinquished have been paid.

SEC. 6. Purchase of materials, etc., on termination of lease.—Upon the expiration of this lease, or the earlier termination thereof pursuant to the last proceeding section, the lessor or another lessee may, if the lessor shall so elect within 3 months from the termination of the lease, purchase

all materials, tools, machinery, appliances, structures, and equipment placed in or upon the land by the lessee, and in use thereon as a necessary or useful part of an operating or producing plant, on the payment to the lessee of such sum as may be fixed as a reasonable price therefor by a board of three appraisers, one of whom shall be chosen by the lessor, one by the lessee, and the other by the two so chosen; pending such election all equipment shall remain in normal position. If the lessor, or another lessee, shall not within 3 months elect to purchase all or any part of such materials, tools, machinery, appliances, structures, and equipment, the lessee shall have the right at any time, within a period of 90 days thereafter to remove from the premises all the material, tools, machinery, appliances, structures, and equipment which the lessor shall not have elected to purchase, save and except casing in wells and other equipment or apparatus necessary for the preservation of the well or wells. Any materials, tools, machinery, appliances, structures, and equipment, including casing in or out of wells on the leased lands, shall become the property of the lessor, on expiration of the period of 90 days above referred to or such extension thereof as may be granted on account of adverse climatic conditions throughout said period.

SEC. 7. Proceedings in case of default.—If the lessee shall not comply with any of the provisions of the act or the regulations thereunder or make default in the performance or observance of any of the terms, covenants, and stipulations hereof and such default shall continue for a period of 30 days after service of written notice thereof by the lessor, the lease may be canceled by the Secretary of the Interior in accordance with section 31 of the act, as amended, and all materials, tools, machinery, appliances, structures, equipment, and wells shall thereupon become the property of the lessor, except that if said lease covers lands known to contain valuable deposits of oil or gas, the lease may be canceled only by judicial proceedings in the manner provided in

section 31 of the act; but this provision shall not be construed to prevent the exercise by the lessor of any legal or equitable remedy which the lessor might otherwise have. A waiver of any particular cause of forfeiture shall not prevent the cancellation and forfeiture of this lease for any other cause of forfeiture, or for the same cause occurring at any other time.

SEC. 8. Heirs and successors in interest.—It is further covenanted and agreed that each obligation hereunder shall extend to and be binding upon, and every benefit hereof shall inure to, the heirs, executors, administrators, successors, or assigns of the respective parties hereto.

SEC. 9. Unlawful interest.—It is also further agreed that no Member of, or Delegate to, Congress, or Resident Commissioner, after his election or appointment, or either before or after he has qualified, and during his continuance in office, and that no officer, agent, or employee of the Department of the Interior, shall be admitted to any share or part in this lease or derive any benefit that may arise therefrom; and the provisions of section 3741 of the Revised Statutes of the United States, and sections 114, 115, and 116 of the Codification of the Penal Laws of the United States approved March 4, 1909 (35 Stat. 1109), relating to contracts, enter into and form a part of this lease so far as the same may be applicable.

IN WITNESS WHEREOF:

THE UNITED STATES OF AMERICA.

~~By~~ /s/ [illegible]

For the Director of the Bureau of Land Management.

[Blank signature blocks]

**Schedule "A"**

**RENTALS AND ROYALTIES**

*Rentals.*—To pay the lessor an advance on the first day of the month in which the lease issues a rental at the following rates:

*(a)* If the lands are wholly outside the known geologic structure of a producing oil or gas field:

(1) For the first lease year, a rental of 50 cents per acre.

(2) For the second and third lease years, no rental.

(3) For the fourth and fifth years, 25 cents per acre.

(4) For the sixth and each succeeding year, 50 cents per acre.

*(b)* On leases wholly or partly within the geologic structure of a producing oil or gas field:

(1) Beginning with the first lease year after 30 days' notice that all or part of the land is included in such a structure and for each year thereafter, prior to a discovery of oil or gas on the lands herein, $1 per acre.

(2) On the lands committed to an approved cooperative or unit plan which includes a well capable of producing oil or gas and contains a general provision for allocation of production, for the lands not within the participating area an annual rental of 50 cents per acre for the first and each succeeeding lease year following discovery.

*Minimum royalty.*—To pay the lessor in lieu of rental at the expiration of each lease year after discovery a minimum royalty of $1 per acre or, if there is production, the difference between the actual royalty paid during the year and the prescribed minimum royalty of $1 per acre, provided that on unitized leases, the minimum royalty shall be payable only on the participating acreage.

*Royalty on production.*—To pay the lessor 12½ percent royalty on the production removed or sold from the leased lands.

The average production per well per day for oil and for gas shall be determined pursuant to 30 CFR, Part 221, "Oil and Gas Operating Regulations."

In determining the amount or value of gas and liquid products produced, the amount or value shall be net after an allowance for the cost of manufacture. The allowance for cost of manufacture may exceed two-thirds of the amount or value of any product only on approval by the Secretary of the Interior.

IN THE

# Supreme Court of the United States

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BP AMERICA PRODUCTION COMPANY, SUCCESSOR IN INTEREST TO AMOCO PRODUCTION COMPANY, *et al.*,
*Petitioners,*

v.

REBECCA W. WATSON, ASSISTANT SECRETARY, LAND AND MINERALS MANAGEMENT, DEPARTMENT OF THE INTERIOR, *et al.*,
*Respondents.*

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**On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit**

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No. 05-669

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April 17, 2006

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Petition for writ of certiorari to the United States Court of Appeals for the District of Columbia Circuit granted limited to Question 2 presented by the petition.

The Chief Justice and Justice Breyer took no part in the consideration or decision of this petition.

(b)

No. 05-669

Supreme Court, U.S.
FILED
6/13/2006
JUN 13 2006
OFFICE OF THE CLERK

IN THE

# Supreme Court of the United States

BP AMERICA PRODUCTION COMPANY AND
ATLANTIC RICHFIELD COMPANY,
*Petitioners,*

v.

REJANE BURTON,
ACTING ASSISTANT SECRETARY OF THE INTERIOR
FOR LAND AND MINERALS MANAGEMENT, *et al.*,
*Respondents.*

**On Writ of Certiorari**
**to the United States Court of Appeals**
**for the District of Columbia Circuit**

## BRIEF FOR PETITIONERS

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## QUESTION PRESENTED

Whether the limitations period in 28 U.S.C. § 2415(a) applies to federal agency orders requiring the payment of money claimed under a lease or other agreement.

## LIST OF PARTIES AND PARTIES TO THE PROCEEDINGS BELOW

Petitioner BP America Production Company is the successor in interest to Amoco Production Company and Vastar Resources, Incorporated. Petitioner Atlantic Richfield Company, along with Amoco Production Company and Vastar Resources, Incorporated, were appellants in the court of appeals and plaintiffs in the district court.

Respondents are Rejane Burton, in her capacity as Acting Assistant Secretary of the Interior for Land and Minerals Management; Dirk Kempthorne, in his capacity as Secretary of the Interior; Southern Ute Indian Tribe; Assiniboine and Sioux Tribes of the Fort Peck Indian Reservation; Burlington Resources Inc.; Steve Westly, in his capacity as California State Controller; Jicarilla Apache Nation; the State of Colorado; and the State of New Mexico.

Respondent Kempthorne is the successor to Gale Norton, who was respondent in this Court, appellee in the court of appeals, and defendant in the district court. She is the successor to Bruce Babbitt, who was defendant in the district court. Respondent Burton is the successor to Rebecca W. Watson, who was appellee in the court of appeals. Watson was the successor to Wallace P. DeWitt, who was defendant in the district court. DeWitt was the successor to Sylvia V. Baca, who was defendant in the district court.

Respondent Southern Ute Indian Tribe was an intervenor supporting appellees in the court of appeals and an intervenor supporting defendants in the district court. Respondents Assiniboine and Sioux Tribes of the Fort Peck Indian Reservation; Steve Westly, in his capacity as California State Controller; Jicarilla Apache Nation; the State of Colorado; and the State of New Mexico, by and through the State of New Mexico Office of the Attorney General, were all intervenors supporting appellees in the court of appeals. Respondent Burlington Resources Inc. was an intervenor supporting the appellants in the court of appeals.

## CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.6 of the Rules of this Court, petitioners BP America Production Company and Atlantic Richfield Company state the following:

On December 31, 2001, Amoco Production Company and Vastar Resources, Inc. merged and formed BP America Production Company. BP America Production Company is wholly owned by BP Company North America Inc. BP Company North America Inc. is wholly owned by BP Corporation North America Inc. BP Corporation North America Inc. is wholly owned by BP America Inc. Atlantic Richfield Company is wholly owned by BP America Inc.

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IN THE

# Supreme Court of the United States

No. 05-669

BP AMERICA PRODUCTION COMPANY AND
ATLANTIC RICHFIELD COMPANY,
*Petitioners*,

v.

REJANE BURTON,
ACTING ASSISTANT SECRETARY OF THE INTERIOR
FOR LAND AND MINERALS MANAGEMENT, *et al.*,
*Respondents.*

**On Writ of Certiorari to the
United States Court of Appeals
for the District of Columbia Circuit**

## BRIEF FOR PETITIONERS

### OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-20a) is published at 410 F.3d 722 (D.C. Cir. 2005). The opinion of the district court (Pet. App. 21a-56a) is published at 300 F. Supp. 2d 1 (D.D.C. 2003). The September 12, 2000, decision of the Department of Interior's Minerals Management Service (Pet. App. 68a-97a), and the May 27, 1997, Minerals Management Service Letter Order to Amoco Production Company (Pet. App. 144a-156a), are unreported.

### JURISDICTION

The judgment of the court of appeals was entered on June 10, 2005. The court of appeals denied a petition for rehearing on August 24, 2005 (Pet. App. 175a). The petition for a writ of certiorari was filed on November 22, 2006, and granted, limited to Question 2, on April 17, 2006. J.A. 24. This Court has jurisdiction under 28 U.S.C. § 1254(1).

## STATUTORY PROVISIONS INVOLVED

Section 2 of the Act of July 18, 1966, Pub. L. No. 89-505, 80 Stat. 304, codified as amended at 28 U.S.C. § 2415 *et seq.*, is set forth in its entirety in the Appendix to the Petition for a Writ of Certiorari, Pet. App. 179a-182a, and in the Appendix to this brief, App., *infra*, 1a-4a. In relevant part, it provides:

> (a) Subject to the provisions of section 2416 of this title, and except as otherwise provided by Congress, every action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later * * * .
>
> * * * * *
>
> (i) The provisions of this section shall not prevent the United States or an officer or agency thereof from collecting any claim of the United States by means of administrative offset, in accordance with section 3716 of title 31.

28 U.S.C. § 2415(a), (i).

## STATEMENT

The six-year statute of limitations codified at 28 U.S.C. § 2415(a) applies to "every action for money damages brought by the United States * * * which is founded upon any contract" except administrative offsets, which are expressly excluded. The question in this case is whether Section 2415(a) otherwise applies to administrative actions founded on contract, such as actions for past-due royalties claimed under federal leases for oil and gas properties.

## I. Statutory Background

A. The Mineral Leasing Act of 1920 ("MLA"), 30 U.S.C. § 181 *et seq.*, authorizes the Secretary of the Interior to lease public-domain lands to private parties for oil and gas production. See 30 U.S.C. § 226(a) (providing that "lands subject to disposition under this chapter which are known or believed to contain oil or gas deposits may be leased by the Secretary"). To that end, the MLA establishes competitive and non-competitive means of awarding leases, and specifies certain mandatory and prohibited lease terms and conditions. See, *e.g.*, 30 U.S.C. §§ 223, 226. Lessees must pay the royalty established in the lease, which cannot be less than "12½ per centum in amount or value of production removed or sold from the lease." 30 U.S.C. § 226(b)(2)(A)(ii).

Since 1911, actions by private parties *against the United States* for breach of contractual obligations, such as lease agreements, have been subject to a six-year statute of limitations. See Act of March 3, 1911, 36 Stat. 1093, codified as amended at 28 U.S.C. § 2401 (providing that "every civil action commenced against the United States shall be barred unless the complaint is filed within six years after the right of action first accrues"). By contrast, until 1966, there was no general statute of limitations governing actions *by the United States* against private parties for breach of the same agreements. Instead, those suits ordinarily were governed by the rule *quod nullum tempus occurrit regi*—"no time shall run against the King"—and the United States had an infinite amount of time within which to seek recovery. The United States was generally "exempt from the consequences of its laches, and from the operation of statutes of limitations." *Guar. Trust Co. of N.Y.* v. *United States*, 304 U.S. 126, 132 (1938); see also *Phillips* v. *Comm'r*, 283 U.S. 589, 602-603 (1931). Thus, even with respect to a single contract, private claims against the government were subject to a six-year limitations period, but government claims against the

private party would persist in perpetuity. See Sen. Rep. No. 1328, 89th Cong., 2d Sess., 11-12 (1966).

To address that disparity, in 1966 Congress enacted 28 U.S.C. § 2415, "a statute aimed at equalizing the litigative opportunities between the Government and private parties." *Crown Coat Front Co.* v. *United States*, 386 U.S. 503, 521 (1967). As the Senate Report accompanying that legislation observed:

> Many of the contract and tort claims asserted by the Government are almost indistinguishable from claims made by private individuals against the Government. Therefore it is only right that the law should provide a period of time within which the Government must bring suit on claims just as it now does as to claims of private individuals. * * * [E]quality of treatment in this regard * * * is required by modern standards of fairness and equity.

Sen. Rep. No. 1328, *supra*, at 2.

The Senate Report also stated that "[m]ore limitations appear[ed] desirable" for a variety of practical reasons. Sen. Rep. No. 1328, *supra*, at 12. Such limitations periods have the "salutary effect" of ensuring that "necessary witnesses, documents, and other evidence are still available," and that the memories of "witnesses are better." *Id.* at 2. "Even if the passage of time does not prejudice the effective presentation of a claim," the Report stated, "the mere preservation of records on the assumption that they will be required * * * increases the cost of keeping records." *Ibid.* The imposition of a limitations period also enhances governmental efficiency by encouraging agencies and government employees to pursue claims promptly. *Id.* at 12.

Section 2415 provides limitations periods for actions founded on contract, arising in tort, and for money erroneously paid. 28 U.S.C. § 2415(a), (b), (d). With respect to actions founded on contract, it provides:

> [E]very action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract * * * shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later.

28 U.S.C. § 2415(a).

Section 2415 also provides an exception to permit the government to assert claims by counterclaim or offset where it is a defendant in litigation. Under Section 2415(f), the limitations period does not prevent "the assertion, in an action against the United States" or its officers, "of any claim of the United States" or its officers "against an opposing party, a co-party, or a third-party that arises out of the [same] transaction." 25 U.S.C. § 2415(f). For claims arising out of different transactions, Section 2415(f) provides that otherwise time-barred claims can "be asserted only by way of offset and may be allowed in an amount not to exceed the amount of the opposing party's recovery." *Ibid.*

Section 2415 separately addresses *administrative* offsets (offsets the government makes, absent litigation, against its debts to reduce or eliminate the amounts it will pay). In particular, Section 2415(i) exempts administrative offsets from Section 2415's limitations period entirely: "The provisions of this section," it declares, "shall not prevent the United States or an officer or agency thereof from collecting any claim of the United States by means of administrative offset, in accordance with section 3716 of title 31." 28 U.S.C. § 2415(i). That provision was added in 1982 as part of the Debt Collection Act of 1982, Pub. L. No. 97-365, 96 Stat. 1749, 1754. At the same time, Congress established a separate 10-year limitations period for administrative offsets, 96 Stat. 1754, which now appears at 31 U.S.C. § 3716(c)(1).

B. Since enacting Section 2415 in 1966, Congress has repeatedly revised it. For example, Section 2415(g) provides that all claims that accrued before Section 2415's enactment are deemed to have accrued on the date of its enactment. 28 U.S.C. § 2415(g). As the six-year limit approached in 1972, however, the agencies responsible for pursuing contract claims on behalf of Indian tribes advised Congress that, absent an extension, many such claims would be barred. As a result, Congress enacted a series of provisos to extend the time for such claims, starting with a proviso affording them an additional 90 days. See, *e.g.*, Act of July 18, 1972, Pub. L. No. 92-353, 86 Stat. 499, codified at 28 U.S.C. § 2415(a) (second proviso). Lawyers representing several tribes explained to Congress that a further amendment was necessary to preserve, among others, a significant number of claims arising from "violations of lease agreements." *Time Extension For Commencing Actions on Behalf of Indians: Hearing before the Subcomm. on Indian Affairs of the S. Comm. on Interior and Insular Affairs*, 92d Cong., 2d Sess. 38 (1972) (joint statement of Arthur Lazarus, Jr., Martin J. Sonosky, and Charles A. Hobbs). Congress therefore extended the limitations period for pre-1966 Indian claims again, this time by five years. Act of Oct. 13, 1972, Pub. L. No. 92-485, 86 Stat. 803. Eventually, Congress established a system under which the limitations period for any claim arising before Section 2415's enactment would not be barred until a specified period after the Secretary of the Interior publishes the claim. See Indian Claims Limitation Act of 1982, § 2(a), 96 Stat. 1976, codified at 25 U.S.C. § 2415(a) (third and fourth provisos).

Most recently, Congress prospectively adopted a seven-year limitations period for any "judicial proceeding or demand" relating to royalties under a federal oil and gas lease. Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 ("FOGRSFA"), Pub. L. No. 104-185, 110 Stat. 1700, codified at 30 U.S.C. § 1724(b). The new provision, however, does not address the limitations period for

Indian claims, claims under oil and gas leases pertaining to production before September 1, 1996, or claims under federal leases for other minerals. Those continue to be governed by Section 2415. FOGRSFA also adjusted applicable record-retention requirements. The MLA previously required lessees to retain records for six years—the limitations period for government claims—unless the Secretary directed lessees to retain them longer. See 30 U.S.C. § 1713(a) (1983). FOGRSFA changed the record-retention period to correspond with the new limitations periods, requiring lessees to retain records for "the same period of time during which a judicial proceeding or demand may be commenced under * * * this section." 30 U.S.C. § 1724(f).

## II. Proceedings In This Case

### A. The Lease And Proceedings Before The Secretary

About a half-century ago, Amoco Production Company ("Amoco") entered into leases with the Secretary of the Interior for the production of oil and natural gas in New Mexico's San Juan Basin. J.A. 10-23.[1] The leases included bonding requirements; imposed record-keeping requirements; and mandated that Amoco keep its records and premises open for inspection. *Id.* at 11, 14. The leases also required Amoco to pay a "12½ percent royalty on the production removed or sold from the leased lands." *Id.* at 23. Consistent with 60 years of Department of Interior and Minerals Management Service ("MMS") practice, Amoco calculated the royalty as a percentage of the "value of production * * * from the lease" by determining the value of the gas as produced "at the wells." See *Indep. Petroleum Ass'n of Am.* v. *Armstrong*, 91 F. Supp. 2d 117, 125 (D.D.C. 2000), rev'd in part, aff'd in part, 279 F.3d 1036 (D.C. Cir. 2002); Pet. 15-23.

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[1] Petitioner BP America Production Company is Amoco's successor in interest. References to Amoco encompass Amoco and its predecessors in interest.

On April 22, 1996, MMS issued a "Dear Operator/Payor" Letter to producers of coalbed methane gas in the vicinity of New Mexico's San Juan Basin, including Amoco. Pet. App. 170a-174a. The 1996 Payor Letter provided new "guidelines" to producers on how to report and pay royalties on coalbed methane. *Id.* at 170a. Among other things, the letter directed that royalties be based not on the value of gas as produced at the well, but on the enhanced value the gas acquires, after transportation to off-site treatment facilities, when the gas is treated to meet the quality requirements for further transportation in mainline pipelines. The government thus rejected the former practice of calculating royalties on the lesser value of untreated gas as produced at the lease site. *Id.* at 170a-171a.[2]

On May 27, 1997, MMS issued an order directing Amoco to pay additional royalties based on an audit conducted by the State of New Mexico. The order asserted that Amoco had not computed its royalty payments for the period from January 1989 through December 1996 in accordance with the standards set forth in the 1996 Payor Letter. Pet. App. 144a-156a. The order informed Amoco that "[a]ppropriate

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[2] MMS's 1988 regulations provide that the "value of production" shall not "be less than the gross proceeds accruing to the lessee for residue gas and/or any gas plant products, less applicable transportation allowances and processing allowances." 30 C.F.R. § 206.153(h). The regulations allow certain deductions for transporting the gas, *id.* § 206.157, and for certain aspects of processing, *id.* § 206.158. They also provide that the "lessee is required to place residue gas and gas plant products in marketable condition at no cost to the Federal Government." *Id.* § 206.153(i). "Marketable condition" is defined as products "sufficiently free from impurities and otherwise in a condition that they will be accepted by a purchaser under a sales contract typical for the field or area." *Id.* § 206.151. For the first time, the 1996 Payor Letter construed the "marketable condition" regulations to require lessees to incur the cost of processing gas to meet the quality requirements of mainline pipelines used to transport gas to distant end-use markets; formerly, the gas was considered in marketable condition if sufficiently free of impurities to be sold to purchasers on or near the well.

late payment charges pursuant to 30 C.F.R. § 218.102 (1996) will be computed and billed to Amoco upon receipt of payment of the additional royalties due." Pet. App. 154a. It cautioned that "failure to comply with the terms of this order may be considered a violation" that could result in "civil penalties." *Ibid.* Finally, it notified Amoco that it had "the right to appeal in accordance with the provisions of 30 C.F.R. Part 290 (1996)." *Ibid.*

Amoco appealed MMS's order to the Department of Interior. Amoco disputed MMS's interpretation of the royalty regulations; urged that the 1996 Payor Letter was issued and applied in violation of the Administrative Procedures Act; and argued that the demand for any royalties that accrued more than six years before the MMS order's issuance was barred by the limitations period in 28 U.S.C. § 2415(a). See Admin. R. 0316. The Assistant Secretary denied most of Amoco's appeal. Pet. App. 68a-97a. With respect to the statute of limitations, the Assistant Secretary asserted that "[t]his proceeding is an administrative appeal and the statutory bar [in 28 U.S.C. § 2415(a)] is inapplicable." *Id.* at 96a.

**B. Proceedings In District Court**

Amoco, along with Atlantic Richfield Company and Vastar Resources ("ARCO/Vastar") (which had received a similar MMS order on January 27, 1997), sought review of the decisions in the United States District Court for the District of Columbia. On cross-motions for summary judgment, the district court ruled in favor of the government. Pet. App. 21a-56a. Although the district court found that MMS's construction of its royalty valuation requirements was "somewhat circuitous," *id.* at 32a, the court upheld that construction because it was reasonable, *id.* at 39a-40a.

On the statute-of-limitations issue, the district court held that Section 2415(a) does not foreclose the collection of additional royalties accruing more than six years before the May 27, 1997, MMS Order. Pet. App. 48a-55a. The court acknowledged a split of authority on whether Section

2415(a)'s limitations period applies to administrative actions. *Id.* at 52a. The district court declined to follow the Tenth Circuit's *en banc* holding in *OXY USA, Inc.* v. *Babbitt*, 268 F.3d 1001 (2001), that Section 2415(a) does apply to administrative proceedings. Instead, it followed its earlier decision in *Samedan Oil Corp.* v. *Deer*, No. 94-2123, 1995 WL 431307 (D.D.C. June 14, 1995), rev'd on other grounds, *Indep. Petroleum Ass'n of Am.* v. *Babbitt*, 92 F.3d 1248, 1260 (D.C. Cir. 1996), to hold that the limitations period in 28 U.S.C. § 2415(a) does not bar agency actions to impose and collect additional royalties (along with associated interest) in administrative proceedings. Pet. App. 55a.

**C. The D.C. Circuit's Decision**

Amoco and ARCO/Vastar appealed, and the D.C. Circuit affirmed. Pet. App. 1a-20a. With respect to the royalty-valuation issue, the D.C. Circuit acknowledged that Amoco and ARCO/Vastar had "present[ed] a textually plausible reading" of the statute, but held that it was required to defer to Interior's contrary interpretation. Pet. App. 8a-9a. The D.C. Circuit likewise rejected the argument that the 1996 Payor Letter violated the APA. *Id.* at 15a-16a.

Turning to the statute of limitations, the D.C. Circuit held that Section 2415(a) does not apply to MMS orders assessing additional royalties. Pet. App. 16a-20a. The D.C. Circuit observed that "the statute as a whole is admittedly less [than] clear." *Id.* at 17a. Nonetheless, the court concluded that Section 2415's use of the phrase "action for money damages" and the word "complaint" suggest that it was meant to apply only to actions brought in court and to exclude actions before administrative agencies. *Ibid.* Relying on the definition of the words "action" and "complaint" from *Black's Law Dictionary* in particular, the D.C. Circuit declared that "[t]he phrase 'action for money damages' points strongly to a suit in a court of law," and the term "complaint" should be construed as "an 'initial pleading' under 'codes or Rules of Civil Procedure' that contains, *inter*

*alia*, a 'statement of the grounds upon which the *court's* jurisdiction depends.'" *Id.* at 16a-17a (quoting *Black's Law Dictionary* 285 (6th ed. 1990)).

The D.C. Circuit acknowledged that its construction rendered another provision of Section 2415—Section 2415(i)'s exception for collections "by means of administrative offset"—superfluous. Pet. App. 17a-18a. The court of appeals thus did not dispute that, if Section 2415 did not apply to administrative actions generally, "there would have been no need to except administrative offsets in subsection (i)." *Id.* at 18a. It agreed that courts should "construe a statute so as to give effect to 'every clause and word'" whenever possible. *Ibid.* And it acknowledged that other courts, for that very reason, had interpreted Section 2415(a) as extending to administrative actions as well as actions filed in court. *Ibid.* (citing *OXY USA*, *supra*, and *United States* v. *Hanover Ins. Co.*, 82 F.3d 1052 (Fed. Cir. 1996)).

The D.C. Circuit nonetheless parted company with those decisions. It held that, in the circumstances of this case, it was permissible to render subsection (i) superfluous because that provision had been added "to moot a debate between the Justice Department and the Comptroller General about the reach of subsection 2415(a) in the context of administrative offsets." Pet. App. 18a. The court concluded that Congress had added Section 2415(a) to make the statute "crystal clear rather than just clear" in that context. *Id.* at 19a (internal quotation marks omitted). The court of appeals also stated that "statutes of limitations against the sovereign are to be strictly construed." *Ibid.*

## SUMMARY OF ARGUMENT

I. A. Recognizing that it is neither fair nor efficient to expose everyone doing business with the government to damages claims in perpetuity, Congress in 1966 established a comprehensive set of limitations periods applicable to government damages actions sounding (among other things) in contract. In establishing that statute of limitations, Con-

gress used expansive terms: "*[E]very action* for money damages brought by the United States * * * which is founded upon *any* contract," the statute declares, is "barred unless the complaint is filed within six years after the right of action accrues * * * ." 28 U.S.C. § 2415(a) (emphasis added).

Focusing primarily on the definitions of "action" and "complaint," the D.C. Circuit in this case declared that Section 2415(a) should be read as addressing only actions in court. Thus, in the D.C. Circuit's view, the passage of six years may bar the claim's assertion in court, but the government can assert precisely the same claim for the same relief in administrative proceedings in perpetuity. That, of course, is wholly at war with the statute's purpose and destroys the repose Section 2415(a) was supposed to provide. It is also in serious tension with Congress's decision to employ the facially broad terms "every action" and "complaint" in the statute, terms that are sufficiently capacious to encompass the initiation of adversarial proceedings for the recovery of money before administrative agencies and judicial bodies alike. Indeed, the decisions of this Court, numerous Acts of Congress, and a wealth of agency regulations all use the terms "action" and "complaint" to refer to proceedings before administrative agencies.

B. Refusing to give those terms their full sweep here would violate "a cardinal principle of statutory construction"—that courts "must give effect, if possible, to every clause and word of a statute." *Williams* v. *Taylor*, 529 U.S. 362, 404 (2000) (internal quotation marks omitted). As the D.C. Circuit observed, Section 2415(i) provides that the limitations period otherwise imposed by Section 2415(a) shall not prevent the United States from "collecting any claim * * * by means of administrative offset." Pet. App. 51a. If Section 2415 did not limit administrative actions in the first place, that exception for administrative offsets would be superfluous. This Court's cases "express a deep reluctance to interpret a statutory provision so as to render

superfluous other provisions in the same enactment." *Pennsylvania Dep't of Pub. Welfare* v. *Davenport*, 495 U.S. 552, 562 (1990).

C. Construing Section 2415(a) to exclude administrative actions is also at odds with the statutory structure. Section 2415 establishes a general six-year limitations period for government contract claims. But it then provides for more favorable treatment of administrative offsets through which the government may, in satisfaction of a debt owed to it, *retain* money it would otherwise owe: As noted above, Section 2415(i) excepts administrative offsets from the six-year period in favor of a more lenient 10-year limitations period. The D.C. Circuit's construction would accord administrative actions to *exact* money from private individuals even more favorable treatment, subjecting them to no limitations period whatsoever. There is simply no logical reason why Congress would have wanted to provide a six-year limit for *lawsuits to coerce* payment, and a 10-year limit on administrative offsets that allows administrative *withholding of payment*, while subjecting affirmative administrative actions to coerce payments to no limitations period at all. That is also contrary to the pattern elsewhere in Section 2415, which treats offsets and other claims asserted in *response* to a lawsuit more favorably than affirmative efforts to coerce payment. See 28 U.S.C. § 2415(f) (allowing the assertion of an offset where the government is sued, even if the offset would be barred in an action by the government). And it destroys Congress's careful effort to establish a document-retention period that corresponds to the limitations period.

D. Ultimately, the D.C. Circuit's interpretation of Section 2415 guts the very purpose of the statute—the provision of repose. Long ago, this Court observed that allowing "actions of debt" to "be brought at any distance of time" is "utterly repugnant to the genius of our laws." *Adams* v. *Woods*, 6 U.S. (2 Cranch) 336, 342 (1805). Yet that is exactly the consequence of the D.C. Circuit's decision. Al-

though an agency may be barred from bringing a damages action in court after six years, it can seek the exact same relief on the exact same contract in perpetuity through administrative proceedings. The fundamental unfairness of that end-run is compounded by the fact that administrative agencies may collect interest on such claims, even if the delay in seeking payment is entirely attributable to the agency's dereliction. That result also undermines Congress's practical reasons for adopting the limitations period: ensuring that claims are brought only when necessary evidence remains available, reducing record-retention costs, and promoting timely pursuit of government claims. Sen. Rep. No. 1328, 89th Cong., 2d Sess. 2 (1966).

II. The D.C. Circuit's construction is also at odds with Section 2415's origins and history.

A. It was the government's potential use of administrative proceedings to collect stale contract claims that prompted Congress to call for a statute of limitations in the first place. The statute of limitations in Section 2415 should not be construed to provide no relief from the precise abuses that gave rise to its enactment.

B. The final clause of Section 2415's first sentence, moreover, gives agencies additional time when administrative proceedings are required by law. 28 U.S.C. § 2415(a). In particular, agencies have one year following the completion of required proceedings to bring an action in court. In adopting that provision, Congress sought to "toll" the otherwise applicable limitations period. The D.C. Circuit's interpretation, however, would transform that provision into an indefinite statute of limitations for court actions under which the government can evade the six-year limit by delaying the filing of an administrative action for whatever period it wants. Reading such a gaping loophole into the statute is contrary to the "elementary rule of construction that '[an] act cannot be held to destroy itself.'" *Citizens Bank of Md.* v. *Strumpf*, 516 U.S. 16, 20 (1995) (quoting

*Tex. & Pac. R.R. Co.* v. *Abilene Cotton Oil Co.*, 204 U.S. 426, 446 (1907)).

C. The D.C. Circuit's interpretation of Section 2415(a) is also inconsistent with the history of amendments to Section 2415(a). Congress repeatedly found it necessary to amend Section 2415(a) to extend the period for certain Indian contract claims, including mineral and oil and gas leases that could be pursued administratively. If the D.C. Circuit were correct that administrative claims are exempt from Section 2415 and therefore can be brought in perpetuity, there would have been little need for those amendments.

III. Contrary to the United States' position in its response to the petition for a writ of certiorari, an MMS demand for past-due royalties is "founded upon a contract" and seeks "money damages." Br. in Opp. 17 (quoting 28 U.S.C. § 2415(a)). Because the D.C. Circuit did not address those issues, this Court need not address them in the first instance.

A. In any event, MMS's claim derives from the lease, and thus is indisputably "founded on" contract. Indeed, the government has repeatedly stated as much outside the context of litigation, and every court to consider the issue has so concluded.

B. It is equally clear that the government's demand for the payment of past-due money and interest is a claim for compensatory rather than specific relief. It is the quintessential claim for "money damages."

## ARGUMENT

When Congress enacted a statute of limitations for government actions founded on contract, it employed "patently broad" terms. *OXY USA, Inc.* v. *Babbitt*, 268 F.3d 1001, 1005 (10th Cir. 2001) (*en banc*). It provided that "*every* action for money damages brought by the United States * * * which is founded upon *any* contract shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decision shall

have been rendered in applicable administrative proceedings required by contract or by law, whichever is later." 28 U.S.C. § 2415(a) (emphasis added). That language is sufficiently broad to encompass administrative as well as judicial actions to recover damages (past-due payments and interest) under federal leases for mineral-producing properties.

The court of appeals found "the statute as a whole" to be "less clear." Pet. App. 17a. Focusing in particular on the dictionary definitions of two words—"action" and "complaint"—the D.C. Circuit ruled that Section 2415(a) "by its terms, does not cover administrative actions." *Id.* at 19a. But this Court has, for more than a century, "stressed that '[i]n expounding a statute, [the Court] must not be guided by a single sentence or member of a sentence, but look to the provisions of the whole law, and to its object and policy.'" *U.S. Nat'l Bank of Or.* v. *Indep. Ins. Agents of Am., Inc.*, 508 U.S. 439, 455 (1993) (quoting *United States* v. *Heirs of Boisdore*, 49 U.S. (8 How.) 113, 122 (1849)). Construing Section 2415(a) to exclude administrative actions, as the court of appeals did here, would render an entire provision—Section 2415(i)'s exception for administrative offsets—superfluous.

More fundamentally, construing Section 2415(a) to exclude administrative actions is wholly at war with Section 2415's "object and policy." Under that construction, those dealing with the government would confront potential damages claims founded on contract in perpetuity, because the government could always bring an administrative collection action. The construction thus establishes precisely the eternal damages exposure that Section 2415 was meant to eliminate, and wholly eviscerates the repose that Section 2145 was enacted to provide.

## I. Section 2415's Plain Text Encompasses Administrative Proceedings For Contract Royalties

### A. The Words "Action" And "Complaint" Are Commonly Used In Connection With Administrative Proceedings

"To discern Congress' intent," this Court "examine[s] the explicit statutory language and the structure and purpose of the statute." *Ingersoll-Rand Co.* v. *McClendon*, 498 U.S. 133, 138 (1990). Focusing primarily on the definitions of "action" and "complaint" in *Black's Law Dictionary*, the D.C. Circuit held that the language of Section 2415(a), "by its terms, does not cover administrative actions." Pet. App. 16a-17a, 19a. "The phrase 'action for money damages,'" the D.C. Circuit urged, "points strongly to a suit in a court of law," and the term "complaint" should be construed as "an 'initial pleading' under 'codes or Rules of Civil Procedure' that contains, *inter alia*, a 'statement of the grounds upon which the *court's* jurisdiction depends.'" *Id.* at 16a-17a (quoting *Black's Law Dictionary* 285 (6th ed. 1990)).

In ordinary, modern legal usage, however, the terms "action" and "complaint" assuredly are *not* restricted to suits in court. Even a cursory review of this Court's cases, the United States Code, and the Code of Federal Regulations reveals that the words "action" and "complaint" are commonly used in reference to purely administrative proceedings.

1. This Court's cases have often construed the term "action" to encompass administrative actions. In *Pennsylvania* v. *Delaware Valley Citizens' Council for Clean Air*, 478 U.S. 546, 558 (1986), for example, this Court addressed whether the phrase "any action" in Section 304(d) of the Clean Water Act would permit the recovery of attorney's fees and costs incurred in administrative proceedings. The statute provided that a court, "in issuing any final order in any action brought pursuant to * * * this section, may award costs of litigation * * * to any party, whenever the

court determines such award is appropriate." 42 U.S.C. § 7604(d). In that case, the decisions below had awarded fees for administrative proceedings before state agencies and the EPA. Seeking to overturn the award, the Commonwealth of Pennsylvania and the United States (like the D.C. Circuit here) insisted that "the 'actions' contemplated by § 304(d) are judicial actions, not administrative proceedings." *Delaware Valley*, 478 U.S. at 557-558.

This Court "reject[ed] these limiting constructions" on the phrase "any action." *Delaware Valley*, 478 U.S. at 558. The Court agreed that there was a distinction between the language of Section 304(d), which provides for fees in "any action," and the language of 42 U.S.C. § 1988, which provides for fees "'in any action *or proceeding*' * * * ." 478 U.S. at 559 (emphasis added). But the Court refused to attach any significance to that, declaring that "this distinction is not a sufficient indication that Congress intended § 304(d) to apply only to judicial, and not administrative, proceedings." *Ibid.*

In *West* v. *Gibson*, 527 U.S. 212 (1999), this Court again declined to construe the word "action" as limited to judicial, rather than administrative, actions. In that case, the Court considered whether the EEOC could award compensatory damages under an amendment to Title VII that authorized such awards "'[i]n an *action* brought by a complaining party.'" *Id.* at 215 (quoting 42 U.S.C. § 1981a(a)(1)) (emphasis added). Seeking to confine such awards to judicial proceedings, the respondent relied on Congress's use of the word "action," urging that "the word 'action' often refers to judicial cases, not to administrative 'proceedings.'" *Id.* at 220. Examining the statute's text, structure, and purpose, the Court rejected the claim that "by using the word 'action,' Congress intended to deny that compensatory damages is 'appropriate' administrative relief." *Id.* at 220-221.

Consistent with this Court's construction of the term "action," Congress and administrative agencies alike pervasively use the word "action" to denote adversary proceed-

ings before an agency. A variety of statutes use the word "action" to denote administrative proceedings, whether brought to recover money,[3] or otherwise enforce obligations.[4] Still more reflect the common understanding that administrative proceedings are generally called "actions" by using the phrase "administrative action" in contradistinction to "civil action" or "criminal action."[5]

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[3] See, *e.g.*, 42 U.S.C. § 5205(a)(1) (statute of limitations for "administrative action[s] to recover any payment[s] made to a State or local government for disaster or emergency assistance"); 50 U.S.C. app. § 593(f)(1) (provision staying certain "civil or administrative action[s] for damages" based on negligence or liability of a service-member).

[4] See, *e.g.*, 12 U.S.C. § 1441a(b)(11)(G) (requiring Resolution Trust Corporation to maintain staff to assist in certain "cases, civil claims, and administrative enforcement actions"); 15 U.S.C. § 1681s(c)(4) (Fair Credit Reporting Act provision limiting state action during pendency of a federal "civil action" or "administrative action").

[5] See, *e.g.*, 15 U.S.C. § 78u(h)(9)(B) (Securities Exchange Act provision stating that certain "[f]inancial records * * * may be disclosed or used only in an administrative, civil, or criminal action"); 15 U.S.C. § 7212(b)(2)(F) (Sarbanes-Oxley Act provision requiring accounting firms, when applying for registration, to provide "information relating to criminal, civil, or administrative actions or disciplinary proceedings pending against the firm"); 15 U.S.C. § 7706(f)(8) (CAN-SPAM Act provision limiting state action during pendency of a federal "civil action" or "administrative action"); 18 U.S.C. § 3486(e)(1) (Health Insurance Portability and Accountability Act provision that generally prohibits the use of certain health information in "any administrative, civil, or criminal action"); 26 U.S.C. § 7803(d)(1)(G) (Internal Revenue Service Restructuring and Reform Act provision requiring annual report to include "information regarding any administrative or civil actions with respect to violations of the fair debt collection provisions"); 31 U.S.C. § 3729(a)(7)(C) (treble damages unavailable under the False Claims Act if defendant self-reports the false claims while "no criminal prosecution, civil action, or administrative action had commenced * * * with respect to such violation"); 42 U.S.C. § 8512(d)(4) (revocation of state enforcement authority shall not affect certain pending "administrative or civil action[s] or proceeding[s]"); 42 U.S.C. § 8521(g)(2)(C) (similar); 42 U.S.C. § 9622(g)(1) (CERCLA provision setting forth conditions for *de minimus* settlements "in an administrative or civil action").

Likewise, federal agency regulations uniformly recognize that the term "action" may encompass administrative and judicial proceedings alike. Some expressly define the word "action" to mean "any judicial or administrative proceeding." See, *e.g.*, 12 C.F.R. § 545.121(a)(1)(i). Others reflect the common understanding that the word "action" may encompass both by referring to administrative proceedings as "actions,"[6] or referring to "administrative actions" and "judicial actions" in the same breath.[7] Indeed, even as it

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[6] 7 C.F.R. § 3018.400(c) (Dep't of Agric.) (discussing "administrative action[s] for the imposition of a civil penalty" for failure to file disclosure forms); 10 C.F.R. § 601.400(c) (Dep't of Energy) (similar); 12 C.F.R. § 411.400(c) (Export-Import Bank) (similar); 12 C.F.R. § 1412.2(l)(1) (Farm Credit Sys. Ins. Corp.) (defining "prohibited indemnification payment" to include reimbursement for a civil money penalty or judgment resulting from "any administrative or civil action" instituted by the Farm Credit Administration); 14 C.F.R. § 13.18(a)(1) (FAA) (enforcement procedures applicable to certain "action[s] in which the FAA seeks to assess a civil penalty by administrative procedures"); 31 C.F.R. § 501.703(b) (Treasury Dep't) (administrative process for enforcing Trading With the Enemy Act sanctions an "action"); 10 C.F.R. Pt. 820 App. A, IX.b. (Dep't of Energy) ("Administrative actions, such as determination of award fees where DOE contracts provide for such determinations, will be considered separately from any civil penalties that may be imposed under this Enforcement Policy"); 12 C.F.R. § 359.0(c) (FDIC) (barring insured institutions from indemnifying institution-affiliated parties for costs from certain "administrative or civil enforcement action[s] commenced by any federal banking agency").

[7] 10 C.F.R. § 9.104(a)(10) (Nuclear Reg. Comm'n) (addressing meetings concerning "the Commission's participation in a civil action or proceeding or an action or proceeding before a state or federal administrative agency"); 10 C.F.R. § 51.10(d) (Nuclear Reg. Comm'n) (decisions "initiating or relating to administrative or judicial civil or criminal enforcement actions or proceedings" not subject to Section 102(2) of the National Environmental Policy Act); 15 C.F.R. § 904.2 (Nat'l Oceanic and Atmospheric Admin.) (defining "settlement agreement" as "any agreement resolving all or part of an administrative or judicial action"); 28 C.F.R. § 802.25 (Court Servs. & Offender Supervision Agency for DC) (defining "legal proceeding" as including any "judicial or administrative action"); 32 C.F.R. § 93.3(d) (Dep't of Defense) (defining "litigation" as including all "judicial or administrative actions"); 37 C.F.R. § 104.1 (U.S. Patent

disputes the applicability of Section 2415, the Department of Interior repeatedly describes MMS proceedings to recover past-due royalties as "administrative actions."[8] The Department cannot seriously dispute that the term "action" encompasses administrative proceedings when the Department itself refers to its proceedings as "actions."

2. Nor does Section 2415(a)'s use of the word "complaint" confine its effect to judicial proceedings. To the contrary, the term "complaint" is widely used to describe the instrument that initiates proceedings before an administrative agency (and that, if left unanswered, will result in liability). See, *e.g.*, *Ohio Civil Rights Comm'n* v. *Dayton Christian Sch., Inc.*, 477 U.S. 619, 624 (1986) ("When Dayton failed to respond, the Commission initiated administrative proceedings against it by filing a complaint."); *Andrus* v. *Shell Oil Co.*, 446 U.S. 657, 660 (1980) ("[T]he Department issued administrative complaints alleging that the * * * claims were invalid.").

Congress regularly uses the term "complaint" to refer to any instrument that commences adversarial or quasi-judicial processes before an agency. The Federal Trade Commission Act, for example, provides:

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and Trademark Off.) (defining "legal proceeding" to include all "judicial or administrative actions"); 38 C.F.R. § 14.802(d) (Dep't of Veterans Affairs) (same); 45 C.F.R. § 1201.1(b) (Corp. for Nat'l & Cmty. Serv.) (defining "litigation" as encompassing "all judicial or administrative actions"); 39 C.F.R. § 265.13(c)(13) (United States Postal Serv.) (defining "[t]hird-party action" to include "an action, judicial or administrative").

[8] See, *e.g.*, *Navajo Refining Co.*, 147 IBLA 253, 256 (1999) ("This is an administrative *action* initiated after completion of a contract reconciliation which found that the account had a balance due.") (emphasis added); *W.A. Moncrief, Jr.*, 144 IBLA 13, 15 (1998) ("[A] Departmental proceeding requiring payments that accrued more than 6 years before the proceeding was initiated 'is not an action for money damages * * *, but rather is administrative *action* not subject to the statute of limitations.'") (quoting *Alaska Statebank*, 111 IBLA 300, 311 (1989)) (emphasis added); *Andarko Petroleum Corp.*, 122 IBLA 141, 147 (1992) (same).

> Whenever the Commission shall have reason to believe that any such person * * * is using any unfair method of competition * * * , and if it shall appear to the Commission that a proceeding by it in respect thereof would be to the interest of the public, it shall issue and serve upon such person * * * a *complaint* stating its charges in that respect and containing a notice of a hearing * * * .

15 U.S.C. § 45(b) (emphasis added). A raft of other statutes also use the word "complaint" in that fashion.[9]

Administrative usage is similar. For example, the Federal Labor Relations Authority and the National Labor Relations Board both file a "complaint" to commence unfair labor practice proceedings. See, *e.g.*, 5 C.F.R. § 2423.20(a) (FLRA); 29 C.F.R. § 102.15 (NLRB). A wealth of other regulations likewise use the word "complaint" to refer to the instrument that begins administrative proceedings.[10]

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[9] 29 U.S.C. § 160(b) (National Labor Relations Act provision allowing the NLRB to issue a "complaint" to persons engaging in unfair labor practices); 25 U.S.C. § 2713(a)(3) (Indian Gaming Regulatory Act provision requiring agency to provide tribal operators or management contractors with a "complaint" for certain violations); 15 U.S.C. § 522 (allowing the Secretary of Commerce to issue a "complaint" for monopoly in the fishing industry); 19 U.S.C. § 1337(b)(1) (Tariff Act of 1930 provision allowing agency to investigate violations "on complaint").

[10] 9 C.F.R. § 202.103(a) (Dep't of Agric.) (reparation proceeding under the Packers and Stockyards Act "is begun by filing a complaint"); 10 C.F.R. § 76.7(b) (Nuclear Reg. Comm'n) (declaring that an "administrative proceeding" alleging discrimination for engaging in protected activities "must be initiated * * * by filing a complaint"); 16 C.F.R. § 3.11(a) (FTC) (stating that "an adjudicative proceeding is commenced when an affirmative vote is taken by the Commission to issue a complaint"); 17 C.F.R. § 10.21 (Commodity Futures Trading Comm'n) (declaring that "an adjudicatory proceeding is commenced when a complaint and notice of hearing is filed with the Office of Proceedings"); 20 C.F.R. § 901.35(a) (Joint Bd. for the Enrollment of Actuaries) (stating requirements for a "complaint initiating a suspension or termination proceeding"); 24 C.F.R. § 103.204(a) (Dep't of Hous. and Urban Dev.) (allowing Assistant Secretary to file a "complaint" based on information

Indeed, notwithstanding its position here, the Department of Justice defines the term "adjudicatory proceeding" in part as "an *administrative* judicial-type proceeding * * * *commencing with the filing of a complaint.*" 28 C.F.R. § 68.2 (emphasis added).

Against that backdrop, Congress's use of the word "complaint" in Section 2415(a) cannot be construed to limit the six-year limitations period to judicial, as opposed to administrative, actions. To the contrary, that term encompasses any written instrument that provides notice and commences proceedings, no matter how it is denominated. As various agencies acknowledge, the word "[c]omplaint" in administrative practice "means *any document* initiating an adjudicatory proceeding, *whether designated a complaint or an order* for proceeding *or otherwise.*" 17 C.F.R. § 10.2(f) (emphasis added); see 7 C.F.R. § 1.132 ("Complaint means the formal complaint * * * or other document by virtue of which a proceeding is instituted.").[11]

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that a discriminatory housing practice has occurred); 29 C.F.R. § 458.66(c) (Dep't of Labor) (proceedings to enforce standards of conduct shall be instituted by the "filing [of] a complaint"); 32 C.F.R. Pt. 277 app. at G. (Dep't of Defense) (implementing Program Fraud Civil Remedies Act and discussing the requirements for issuance of an administrative "complaint"); 33 C.F.R. § 20.401 (Coast Guard) (stating that an "administrative proceeding commences when the Coast Guard representative files the complaint"); 39 C.F.R. §952.5 (United States Postal Serv.) (requiring General Counsel to "prepare and file * * * a complaint" to commence proceedings for false representation); 40 C.F.R. § 22.13(a) (Envtl. Prot. Agency) (administrative proceedings for civil penalties and the revocation, termination or suspension of permits are "commenced by filing * * * a complaint"); 41 C.F.R. § 60-30.5(a) (Dep't of Labor) (administrative proceedings to enforce equal opportunity requirements are instituted by the "filing [of] a complaint").

[11] The D.C. Circuit conceded that "some statutes provide for a 'complaint' that triggers administrative proceedings," but distinguished the MMS order at issue here because it was called "an *order*," and because the ensuing adjudication is denominated an "appeal" rather than the initial "adjudicative hearings on the merits." Pet. App. 17a. But that agency-specific view gives too much weight to the arbitrary labels used

3. No less significant than Congress's use of expansive terminology is Congress's decision not to use language that would limit Section 2415(a)'s application to proceedings in court. Where Congress seeks to establish a limitations period that applies solely to judicial proceedings, it ordinarily includes language specific to the judicial process. For example, some federal statutes of limitations refer to a time in which to bring "suit."[12] Others use the phrase "civil action,"

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by Interior (primarily for historic reasons) and misunderstands MMS administrative practice. An agency cannot evade the six-year limitations period simply by calling the document that commences proceedings something other than a "complaint" (or, for that matter, by calling its adjudication of the merits an "appeal"). Even in the judicial context, different jurisdictions have attached different labels to what is often now called the "complaint." At common law, for example, the complaint was called a "declaration." *Black's Law Dictionary* 356 (4th ed. 1968). In Oklahoma state practice, it is called a "petition." Okla. Stat. tit. 12, § 2003. Yet no one would contend that, notwithstanding the statute of limitations, the government could file suit in Oklahoma to recover simply because that jurisdiction uses another word to describe the complaint. As the regulations cited at pages 22-23, *supra*, make clear, the same is true for agencies: In administrative practice, "[c]omplaint means any document initiating an adjudicatory proceeding, whether designated a complaint * * * or otherwise." 17 C.F.R. § 10.2(f). Here, although denominated an "order," the MMS order to pay royalties serves precisely the function of a complaint, which is "to give defendant information of all material facts on which plaintiff relies to support his demand," *Black's Law Dictionary* 356 (4th ed. 1968), and to initiate proceedings for the recovery of royalties. Indeed, MMS regulations do not afford a lessee a hearing on the matters addressed in the order prior to the order's issuance. An "adjudicative hearings on the merits" does follow the filing of the complaint or order, Pet. App. 17a, but that is (for historic reasons) called an "appeal." See 30 C.F.R. § 290.100, *et seq.*

[12] See, *e.g.*, 15 U.S.C. § 714b(c) (provision of the Commodity Credit Corporation Charter Act imposing a six-year statute of limitations for any "suit by or against the Corporation"); 38 U.S.C. § 1984(b) (provision relating to veterans' insurance benefits setting six-year statute of limitations on any "suit"); 43 U.S.C. § 900 (six-year statute of limitations for "[s]uits by the United States to vacate and annul any patent to lands erroneously issued under a railroad or wagon-road grant"); 43 U.S.C.

the same phrase the Federal Rules of Civil Procedure employ to refer to cases filed in court.[13] And a large number of statutes of limitations expressly confine themselves to lawsuits by making the limitation period applicable to suits "in the district court of the United States" or a "court of competent jurisdiction."[14]

Congress did not limit the reach of Section 2415(a) to "judicial actions," "court actions," or suits in a "court of

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§ 1166 (six-year statute of limitations for "[s]uits by the United States to vacate and annul any patent").

[13] See, *e.g.*, 15 U.S.C. § 3006(c) (Interstate Horseracing Act provision setting a three-year limit on any "civil action"); 17 U.S.C. § 507(b) (Copyright Act provision establishing a three-year limitations period for "civil action[s]"); 28 U.S.C. § 2409a(g) (Quiet Title Act provision setting a 12-year limitations period for "[a]ny civil action under this section"); 31 U.S.C. § 3731(b) (False Claims Act limit applicable to "civil action[s]"); 49 U.S.C. § 15905(a) (three-year limitations period for any "civil action to recover charges for transportation or service provided by the carrier").

[14] See, *e.g.*, 5 U.S.C. § 552a(g)(5) (Privacy Act of 1974 provision allowing "[a]n action to enforce any liability" to be brought "in the district court of the United States" within two years); 12 U.S.C. § 1831d(b) (Federal Deposit Insurance Act provision allowing a person who is overcharged interest to recover in "a civil action commenced in a court of appropriate jurisdiction" within two years); 12 U.S.C. § 2614 (Real Estate Settlement Procedures Act of 1974 provision allowing certain "action[s]" to be brought "in the United States district court" within various lengths of time); 15 U.S.C. § 1640(e) (Truth in Lending Act provision allowing "action[s]" against creditors who fail to comply with certain requirements to be brought "in any United States district court" within one year); 15 U.S.C. § 1681p (Fair Credit Reporting Act provision allowing "[a]n action to enforce any liability" under the Act to "be brought in any appropriate United States district court" within five years of the violation or two years of its discovery); 18 U.S.C. § 5408(a) (Fastener Quality Act provision setting a 10-year limitations period for bringing "an action in an appropriate United States district court"); 42 U.S.C. § 3613(a)(1)(A) (Fair Housing Act provision allowing for enforcement by private persons through "a civil action in an appropriate United States district court" within two years of the violation); 42 U.S.C. § 4053 (provision relating to national flood insurance setting a one-year limitations period for instituting an "action" "in the United States district court" against an insurer that refuses a claim).

competent jurisdiction." To the contrary, it enacted a statute that applies to "*every* action." As the Tenth Circuit observed, that language is "patently broad." *OXY USA*, 268 F.3d at 1005. And it is certainly broad enough to encompass judicial actions and administrative actions alike. Even if that were not clear from Congress's use of expansive language like "every action," any ambiguity is eliminated by the remaining canons of statutory construction.

### B. Excluding Administrative Proceedings From Section 2415's Scope Would Render An Entire Provision Of The Statute Superfluous

1. Reading Section 2415 as applicable only to judicial actions would also violate the "'cardinal principle of statutory construction' that 'a statute ought * * * to be so construed that, if it can be prevented, no clause, sentence, or word shall be superfluous, void, or insignificant.'" *TRW Inc.* v. *Andrews*, 534 U.S. 19, 31 (2001) (quoting *Duncan* v. *Walker*, 533 U.S. 167, 174 (2001)). As amended, Section 2415 contains a limited exception for a specific category of administrative actions—administrative offsets. Through such offsets, the United States can collect a debt by withholding money the United States would otherwise pay.[15]

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[15] "Administrative offset" is defined as an agency "withholding funds payable by the United States * * * to, or held by the United States for, a person to satisfy a claim." 31 U.S.C. § 3701(a)(1). The Federal Claims Collection Standards ("FCCS"), currently promulgated jointly by the Department of the Treasury and the Department of Justice at 31 C.F.R. § 900, *et seq.*, exemplify the administrative offset procedure. The FCCS first requires an agency to notify the debtor of the "type and amount of the debt" and its "intention * * * to use administrative offset to collect the debt." *Id.* § 901.3(4)(ii)(A). The debtor must then be given an opportunity "to inspect and copy agency records related to the debt," to obtain "review within the agency of the determination of indebtedness," and "to make a written agreement to repay the debt." *Id.* § 901.3(4)(B)(1)-(3). Once a debt is 180 days delinquent, however, the agency is required to refer the debt to the Secretary of the Treasury for collection. *Id.* § 901.3(b)(1). The Department of Treasury then cross-references the taxpayer identification number ("TIN") of the debtor with the list of

Section 2415(i) in particular provides that the general six-year statute of limitations "shall not prevent the United States or an officer or agency thereof from collecting any claim of the United States *by means of administrative offset*, in accordance with section 3716 of title 31." 28 U.S.C. § 2415(i) (emphasis added).

If Section 2415(a) did not by its terms encompass administrative actions as well as suits in court, then Subsection (i)'s express exception for administrative offsets would serve no purpose whatsoever. See *OXY USA*, 268 F.3d at 1006; *United States* v. *Hanover Ins. Co.*, 82 F.3d 1052, 1055 (Fed. Cir. 1996). Because it is the duty of every court to "give effect, if possible, to every clause and word of a statute," *United States* v. *Menasche*, 348 U.S. 528, 538-539 (1955) (internal quotation marks omitted), it is generally inappropriate to construe a statute so as to render an *entire provision* mere surplusage. This Court regularly declines to read a statutory provision so as to render an express exception "wholly superfluous." *TRW*, 534 U.S. at 31 (quoting *Duncan*, 533 U.S. at 174). Yet that is precisely what the D.C. Circuit's construction does here.

2. The court of appeals agreed that the superfluity principle was "not without force" here. Pet. App. 18a. Nonetheless, that court thought contravention of the principle tolerable in these circumstances, primarily because Subsection (i) was "added more than 16 years after the passage of the original Act" in the context of the Debt Collection Act of 1982. Pet. App. 17a, 18a. But the rule against rendering a statutory provision superfluous is at its apex where the provision is added by amendment. See *Stone* v. *INS*, 514 U.S. 386, 397 (1995). "When Congress acts to amend a statute," the Court "presume[s] it intends its amendment to have a real and substantial effect." *Ibid.* Contrary to the

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payments to be made by the government. *Id.* § 901.3(b)(2). "When the name and TIN of a debtor match the name and TIN of a payee * * * the payment will be offset to satisfy the debt." *Ibid.*

D.C. Circuit's suggestion, moreover, the legislative history of Subsection (i) confirms that Subsection (i) should not be rendered mere surplusage.

The Debt Collection Act was designed "[t]o increase the efficiency of Government-wide efforts to collect debts owed the United States and to provide additional procedures for the collection of debts owed the United States." Pub. L. No. 97-365, 96 Stat. 1749. To that end, the Debt Collection Act anticipated expansive use of the administrative offset procedure, and Section 10 set forth new guidelines and procedures for its use. 96 Stat. 1754-1755. Before the Debt Collection Act's passage, however, "[a] Justice Department ruling * * * prevent[ed] agencies from using" an "administrative offset beyond the six year statute of limitations" in Section 2415(a). *Collection of Debts Owed the United States: Hearings on H.R. 4614 Before the Subcomm. on Admin. Law and Gov't Relations of the H. Comm. on the Judiciary*, 97th Cong., 2d Sess. 16 (1982) (statement of Joseph R. Wright, Jr., Deputy Dir. Off. of Management and Budget). In particular, the Office of Legal Counsel had ruled that government agencies cannot "collect by 'administrative offset' Government claims, which cannot be pursued in court because of a statute of limitations." *Effect of Statute of Limitations on Administrative Collection of United States Claims*, Mem. Op. Off. Legal Counsel 1 (Sept. 29, 1978).[16] The opinion noted that, at the time, Section 2415(f) provided the only "exception to the general rule that the Government cannot bring an action on a time-barred debt." *Id.* at 5. Under Subsection (f), the United States could assert an otherwise time-barred claim as a counterclaim or by way of offset, but only in response to "an action against the United States" brought by the debtor. 28 U.S.C. § 2415(f). After evaluating that exception, the Office

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[16] Although cited in the legislative record, the Office of Legal Counsel opinion appears to be unpublished. Consistent with this Court's Rule 32.3, petitioners will lodge a copy with the Court upon request.

of Legal Counsel concluded that it was "clear that the Government may not administratively collect a time-barred debt by withholding money from a designated payee," unless that payee has "prevailed on a claim against the United States." Mem. Op. Off. of Legal Counsel, *supra*, at 6.

The Office of Legal Counsel urged that a contrary reading would also be at odds with the statutory structure and purpose. First, the exception contained in Section 2415(f) rested on the notion that, "[b]y initiating the claim the [plaintiff] embroils himself in a controversy against the United States." Mem. Op. Off. of Legal Counsel, *supra*, at 7. Having chosen to "embroil" himself in that controversy, the plaintiff cannot complain if the *entire* controversy is adjudicated. *Ibid.* Accordingly, Section 2415(f) permits the United States to assert otherwise barred counterclaims if they arise from the same transaction as the plaintiff's suit. In addition, by embroiling himself in a lawsuit with the United States, the plaintiff exposes himself to the possibility of an "offset" for claims from unrelated transactions, but only "in an amount not to exceed the amount of the [plaintiff's] recovery." 28 U.S.C. § 2415(f). Allowing the government to recover the full amount of its claim absent a suit against it, the Office explained, was inconsistent with those narrow exceptions. Mem. Op. Off. of Legal Counsel, *supra*, at 7. Indeed, "if the United States could *administratively* collect time-barred debts where no claim were filed against it, this would result in a completely ineffective statute of limitations," and "the repose intended by § 2415 would be illusory." *Ibid.*

Because the Comptroller disagreed with the Office of Legal Counsel's view,[17] Congress eventually enacted Sec-

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[17] The Comptroller General urged that statutes of limitation "run only against the remedy" and "do not discharge the debt." *In the Matter of Collection of Debts—Statute of Limitations on Administrative Offset*, 58 Comp. Gen. 501, 504-505 (1979). In the Comptroller's view, "the government has the right to collect the indebtedness of its employees by means of setoff against monies owed to the employee even if direct

tions 9 and 10 of the Debt Collection Act to resolve the dispute. Section 9 created Subsection (i) to exempt administrative offsets from Section 2415's scope. 96 Stat. at 1754. At the same time, Section 10 established a separate 10-year limitations period to govern administrative offsets. 96 Stat. at 1754, codified at 31 U.S.C. § 3716(e)(1). In so amending the statute, however, Congress necessarily clarified the implications of Section 2415(a) for administrative actions more generally. The "classic judicial task of reconciling many laws enacted over time, and getting them to 'make sense' in combination, necessarily assumes that the implications of a statute may be altered by the implications of a later statute." *United States* v. *Fausto*, 484 U.S. 439, 453 (1988). Once statutes have been amended, they must "be read, as to all subsequent occurrences, as if they had originally been in the amended form." *United States* v. *LaFranca*, 282 U.S. 568, 576 (1931). Here, Congress established a solitary exception for certain administrative actions—administrative offsets—but no others. In so doing, Congress made clear that administrative actions within the exception would be exempted from the limitations period, but actions outside the exception would be covered.

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action to collect the debt would be barred by the statute of limitations." *Id.* at 507. The Comptroller General's position was also contrary to the Joint Committee on Taxation, which summarized the "present law" as follows in its report to Congress: "*Statute of Limitations for Federal Debt Collection.* In general, there is a six-year statute of limitations on Federal debt collection actions. There is no exception for Federal debts collected through administrative offset." *Hearings on S. 1249 Before the Subcomm. on Oversight of the IRS of the S. Comm. on Finance*, 97th Cong., 1st Sess. 24 (1981) (statement of the staff of the Joint Comm. on Taxation). The Comptroller General recommended that Congress enact Subsection (i) "as a means of resolving the differences." *Debt Collection Act of 1981: Hearings on S. 1249 before the Senate Committee on Governmental Affairs*, 97th Cong., 1st Sess. 83 (1981) (statement of Milton J. Socolar, Acting Comptroller General).

### C. The D.C. Circuit's Construction Is Inconsistent With The Statutory Structure And Upsets The Coherence Of The Statutory Scheme

Where possible, this Court must "interpret [a] statute as a symmetrical and coherent regulatory scheme * * * and fit, if possible, all parts into an harmonious whole." *FDA* v. *Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 133 (2000) (internal quotation marks omitted). The D.C. Circuit's crabbed construction of Section 2415 is inconsistent with the symmetry and coherence of this statutory scheme in three distinct respects.

1. *First*, that construction creates unexplained and irrational gaps in the statute. When Congress established the limitations periods in Section 2415, it carefully selected different periods for different types of government claims—*e.g.*, three years for cases arising in tort, and six years for actions for money damages founded on contract. At the same time, Congress also established more liberal rules to govern the government's right to assert claims defensively to minimize its liability in litigation, and administratively (absent litigation) to avoid paying money otherwise due. When the government asserts an administrative offset to avoid paying money, that offset is subject to a more lenient 10-year limitations period. 31 U.S.C. § 3716(e)(1). When a private party initiates an action *against* the government, Section 2415(f) allows the government to assert an offset—including one that would otherwise be time-barred—up to the amount of the plaintiff's recovery. See 28 U.S.C. § 2415(f); p. 5, *supra*.

Construing Section 2415 to exempt administrative actions to recover money damages from any limitations period defies the logic of that scheme. Under that construction, *judicial* actions to *extract* money are subject to a limitations period; *administrative* actions to *withhold* money are subject to a slightly longer one; but *administrative* actions to *extract* money are inexplicably permitted in perpetuity. There is simply no reason why Congress would have intend-

ed such a gaping hole in the statutory structure. Moreover, there is no logical reason why Congress would have wanted to treat offensive efforts to *coerce* payment from the debtor more favorably than the withholding of payment to the debtor. That is contrary to the pattern established in Section 2415, which treats government offsets and claims in *response* to private demands for payment more favorably than the government's affirmative efforts to coerce payment. See 28 U.S.C. § 2415(f) (allowing the assertion of an offset where the government is sued, even if the offset would be barred in an action by the government).

2. *Second*, the D.C. Circuit's exclusion of administrative proceedings from Section 2415(a)'s six-year limitations period also scuttles the congruence that Congress established between the limitations period and the statutory record-retention period for oil and gas lessees. As part of the Federal Oil and Gas Management Act of 1982, Pub. L. 97-451, Jan. 12, 1983, 96 Stat. 2447, codified as amended at 30 U.S.C. § 1701, *et seq.*, Congress required lessees of federal and Indian mineral, oil, and gas properties to "establish and maintain any records, make any reports, and provide any information that the Secretary may * * * reasonably require for the purposes of implementing this chapter or determining compliance with rules or orders under this chapter." 30 U.S.C. § 1713(a). The statute specifically requires that such records "shall be maintained for 6 years after the records are generated," 30 U.S.C. § 1713(b)—the limitations period in Section 2415(a).

When Congress prospectively extended the statute of limitations to seven years for any "judicial proceeding or demand" relating to a federal oil and gas lease as part of the Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 ("FOGRSFA"), Pub. L. 104-185, 110 Stat. 1700, codified at 30 U.S.C. § 1724(b), Congress retained that congruity: It simultaneously amended the recordkeeping requirement to mandate the retention of records for "the same period of time during which a judicial proceeding or

demand may be commenced under * * * this section." 30 U.S.C. § 1724(f). The reasons for linking the record-retention period with the limitations period are obvious—it ensures that the government will have access to the records it may need to establish its claims, and that lessees will have the records they need to defend against any unfounded claims, for so long as such claims may be pursued.

The D.C. Circuit's construction destroys that congruity, allowing the United States to bring administrative actions long after the six-year record-retention requirement has lapsed—indeed, in perpetuity. Lessees that tied their record-retention policies to the six-year period may have long since destroyed the documents relating to pre-1996 royalty payments, and thus can neither substantiate nor refute any MMS claims for payment that may be brought through administrative proceedings. Conversely, any lessees that may still hold records relating to pre-1996 royalty payments may feel obligated to maintain those records indefinitely, for fear that they may need to defend themselves in administrative proceedings years in the future. That is directly contrary to one of Section 2415's purposes, which is to relieve the enormous record-keeping burden that might otherwise run in perpetuity. See pp. 37-38, *infra*. And it upsets the harmony of the statutory scheme, creating exactly the situation Congress sought to avoid when it (on two separate occasions) calibrated the record-retention requirements to the statute of limitations.

3. *Third*, and finally, the D.C. Circuit's exclusion of administrative proceedings from Section 2415(a) also destroys the symmetry that Congress intended to bring to government contract disputes. As this Court has recognized, Section 2415 is "a statute aimed at equalizing the litigative opportunities between the Government and private parties." *Crown Coat Front Co.* v. *United States*, 386 U.S. 503, 521 (1967). Time and again, Congress made clear that Section 2415 was intended to place the government on (mostly) equal footing with private parties by making the

six-year limitations period for private lawsuits applicable to actions brought by the government. There is simply no reason to have two different limitation periods for government and private claims that are "almost indistinguishable from" each other. Sen. Rep. No. 1328, *supra*, at 2; see p. 4, *supra*.

The D.C. Circuit's construction would destroy the symmetry of treatment that Section 2415 seeks to establish. By virtue of Section 2415(a), government contract claims are subject to a six-year limitations period that matches the six-year period that, under 28 U.S.C. § 2401, is applicable to private contract claims against the government. That period also matches the limit imposed by the Contract Disputes Act, which provides that every "claim by a contractor against the government relating to a contract and each claim by the government against a contractor relating to a contract shall be submitted within 6 years after the accrual of the claim." 41 U.S.C. § 605(a).[18] Under the D.C. Circuit's construction, however, administrative actions to recover money damages founded on contract would be uniquely excluded from any limitations period at all, allowing agencies to bring such actions at *any* point in the future, long after a private party's action on the same contract has been barred. That asymmetry—providing infinite time for government administrative contract actions against private parties, but only six years for private parties to seek recovery on the same agreement—is wholly at odds with the principle of "equality of treatment" Congress thought compelled by "modern standards of fairness." Sen. Rep. No. 1328, *supra*, at 2.

4. By contrast, reading Section 2415 consistent with its text to apply to "every action" to recover damages founded on contract—administrative or otherwise—avoids all of those disruptions to the statutory scheme. Only that con-

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[18] The Contract Disputes Act applies to certain categories of contracts but does not cover federal oil and gas leases. See 41 U.S.C. § 602(a).

struction avoids otherwise inexplicable gaps in the statutory coverage. Only that construction preserves the congruence between record-retention requirements and the life span of potential contractual liability. And only that construction ensures the parity of treatment for government and private claims that Congress sought to achieve. In short, only that construction is consistent with the obligation to "fit, if possible, all parts [of the statutory scheme] into an harmonious whole." *Brown & Williamson*, 529 U.S. at 133.

### D. The D.C. Circuit's Construction Destroys Section 2415's Fundamental Purposes

Ultimately, construing Section 2415 to exempt administrative actions seeking money damages under a contract from *any* limitations period is inconsistent not merely with the statutory text. It is also at war with the statute's purpose. It leads to absurd results, saddling private individuals acting in good faith with liability for both principal and decades of accumulated interest obligations on otherwise time-barred debts.

1. The fundamental principle underlying any statute of limitations is that, after some period of time, individuals are entitled to repose. See *Wood* v. *Carpenter*, 101 U.S. 135, 139 (1879) (statutes of limitations "promote repose by giving security and stability to human affairs"). Indeed, one of the guiding principles behind Section 2415 was that, "as a matter of fairness, persons dealing with the Government should have some protection against an action by the Government when the act occurred many years previously." Sen. Rep. No. 1328, *supra*, at 11-12. As then-Assistant Attorney General Douglas explained:

> As a general proposition, potential defendants are entitled eventually to put to one side thoughts of possible suits against them. At some point, and with some exceptions, bygones should be bygones. This thesis underlies the statute of limitations applicable to

> private parties. It should apply with equal force to suits brought by the Government.

*Hearing on H.R. 13652 Before Subcomm. No. 2 of the H. Comm. on the Judiciary*, 89th Cong., 2d Sess. 7 (1966) (statement of John W. Douglas, Assistant Attorney General). In short, like this Court before it, Congress recognized that allowing "actions for debt" to "be brought at any distance of time" is "utterly repugnant to the genius of our laws. In a country where not even [serious crimes] can be prosecuted after a lapse of * * * years, it could scarcely be supposed that an individual would remain forever liable to a pecuniary forfeiture." *Adams* v. *Woods*, 6 U.S. (2 Cranch) 336, 342 (1805).

The D.C. Circuit's construction creates precisely the eternal liability that is both "repugnant to our laws" and to the policies of repose and fairness that formed "the principal basis of" Section 2415. H.R. Rep. No. 1534, 89th Cong., 2d Sess. 8 (1966). Under that construction, an agency could allow the limitations period to run, but nonetheless proceed against a party administratively at any point in perpetuity.[19]

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[19] Section 2415(a), which is applicable to "every action for money damages" "*founded upon any contract*" unless "otherwise provided by Congress," 28 U.S.C. § 2415(a), was clearly intended to serve as a "catch-all" limitations period that relieved Congress of the need to enact a specific limitations period for each type of action that an agency might conceivably bring. Congress has enacted several such "catch-all" statutes of limitations in other contexts to ensure that no type or cause of action slips through the cracks. See, *e.g.*, 18 U.S.C. § 3282(a) ("Except as otherwise expressly provided by law, no person shall be prosecuted, tried, or punished for any offense, not capital, unless the indictment is found * * * within five years next after such offense shall have been committed."); 28 U.S.C. § 1658(a) ("Except as otherwise provided by law, a civil action arising under an Act of Congress * * * may not be commenced later than 4 years after the cause of action accrues."); *id.* § 2462 ("Except as otherwise provided by Act of Congress, an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued * * * .").

The knowledge that one is immune from an action in court is of little consolation to the individual who must worry about being subjected to administrative actions forever. And barring a damages action in court on stale claims hardly promotes fairness if the individual is still subject to identical liability before the administrative agency. "Bygones" can never "be bygones" when the potential for administrative liability forever persists.

The Office of Legal Counsel identified precisely that defect when it rejected the notion of perpetual administrative claims under this statute more than two decades ago: "[I]f the United States could administratively collect time-barred debts where no claim were filed against it," the Office observed, "this would result in a completely ineffective statute of limitations" and "the repose intended by § 2415 would be illusory." Mem. Op. Off. of Legal Counsel, *supra*, at 7-8. "There is a strong presumption against construing a statute so as to render it ineffective." *Ibid.* As a result, the Office of Legal Counsel concluded that Section 2415 "must be interpreted as precluding" *all* actions for the "collection of time-barred debts." *Id.* at 8. For the same reasons, this Court should so conclude as well.

2. The D.C. Circuit's construction also undermines each of the other "salutary" goals that Section 2415 was intended to achieve. First, Section 2415 was designed to ensure that any adjudication would occur at a time when "necessary witnesses, documents, and other evidence are still available," and the memories of "witnesses are better." Sen. Rep. No. 1328, *supra*, at 2. If the United States may bring administrative actions to recover on its contracts at any time, however, nothing would prevent it from pursuing claims long after critical documents have disappeared and witnesses' memories have faded.

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The D.C. Circuit's construction cuts a giant hole in Section 2415(a), converting it from a "catch all" into a "catch little."

Section 2415 was also enacted to eliminate the burden of preserving "records" in perpetuity "on the assumption that they will be required" in connection with a claim in the distant future. Sen. Rep. No. 1328, *supra*, at 2. But the D.C. Circuit's construction destroys that purpose as well. Confronted with the possible need to pursue or defend against aged claims in administrative actions, government agencies and private parties respectively will have to retain documents long after any statutory retention period has lapsed. And the goals of enhancing governmental efficiency and prompt pursuit of claims, *id.* at 12, would be lost as well. There is little pressure for an agency to pursue claims promptly in court when administrative remedies always stand ready. This Court ought not "construe [the statute of limitations] so as to defeat its obvious purpose, which is to encourage the prompt presentation of claims." *United States* v. *Kubrick*, 444 U.S. 111, 117 (1979).

3. The unfairness to private parties that results from excluding administrative proceedings from the six-year limitations period in Section 2415(a) would be troubling in almost any context. Here, however, it is compounded by the fact that the agency may be entitled, and in many cases required, to collect interest on its claim.

The MLA, for example, requires MMS to charge interest "where royalty payments are not received by the Secretary on the date that such payments are due, or are less than the amount due." 30 U.S.C. § 1721(a). That interest, moreover, is not calculated at a lenient rate. Instead, MMS must use the Internal Revenue Code formula for underpaid taxes, see 30 U.S.C. § 1721(a), which is "the Federal short-term rate" *plus* "3 percentage points," 26 U.S.C. § 6621(a)(2).[20] The D.C. Circuit's decision thus would allow MMS to wait indefinitely while interest charges pile up against the

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[20] The federal short-term rate is "the average market yield * * * on outstanding marketable obligations of the United States with remaining periods to maturity of three years or less." 26 U.S.C. § 1274(d)(1)(C)(i).

lessee, eventually dwarfing the original obligation.[21] That does not merely result in inequity. It also perverts the incentives that limitations periods are supposed to establish, making older claims (with more interest) more valuable to the government than more timely ones. And since liability is perpetual, claims for centuries of accumulated interest are hardly unthinkable. Just last Term, the United States urged this Court to reinstate an award of $211 million in prejudgment interest following a 204-year delay in filing suit. See *Cayuga Indian Nation* v. *Pataki*, 165 F. Supp. 2d 266 (N.D.N.Y. 2001) (awarding $211 million in interest for a 204 year delay, *after* a 60 percent reduction), rev'd 413 F.2d 266 (2d Cir. 2005), cert. denied, 126 S.Ct. 2022 (2006).

4. Worse still, such liability could be imposed years after the fact without wrongdoing or negligence. Under the MLA, courts generally defer to MMS's construction of the terms of a lease agreement, as the D.C. Circuit did in this case. Pet. App. 7a-8a. While agencies may not ordinarily change the lease's meaning retroactively, cf. *Bowen* v. *Georgetown Univ. Hosp.*, 488 U.S. 204, 208 (1988), decisions "clarifying an unsettled or confusing area of the law" may be given retroactive application, *Pope* v. *Shalala*, 998 F.2d 473, 483 (7th Cir. 1993); see also *Heimmermann* v. *First Union Mortgage Corp.*, 305 F.3d 1257, 1260 (11th Cir. 2002); *Orr* v. *Hawk*, 156 F.3d 651, 654 (6th Cir. 1998).

As a result, a party to a lease agreement might make payments in good faith under a perfectly reasonable con-

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[21] In a dispute between private parties, the equitable defense of laches could be invoked. *Chapman* v. *Bd. of County Comm'rs*, 107 U.S. 348, 355 (1883); see also *Nat'l R.R. Passenger Corp.* v. *Morgan*, 536 U.S. 101, 121-122 (2002). But the federal government is not subject to the defense of laches. See *United States* v. *Summerlin*, 310 U.S. 414, 416 (1940). In this case, the Department of the Interior specifically rejected ARCO/Vastar's argument that "it would be inequitable to assess late payment interest on royalties due based on a valuation procedure that could not have been anticipated by lessees." Pet. App. 124a.

struction of the lease for years or even decades on end, only to have the agency (as here) "clarify" that more money is due because the methodology was wrong. A statute of limitations helps mitigate any potential unfairness by confining any resulting liability to a finite period. If no statute of limitations exists, however, an agency can effectively "clarify" the rules of the game and seek retroactive payments for decades or centuries of supposed "noncompliance" with the newly clarified rule—plus interest. This Court should not construe Section 2415(a) to "permit plaintiffs who know of the defendant's pattern of activity simply to wait, 'sleeping on their rights,' * * * as the pattern continues and [additional damages] accumulate, perhaps bringing suit only long after the 'memories of witnesses have faded or evidence is lost.'" *Klehr* v. *A.O. Smith Corp.*, 521 U.S. 179, 187 (1997) (quoting *Wilson* v. *Garcia*, 471 U.S. 261, 271 (1985)). Such "absurd results are to be avoided," especially where, as here, "alternative interpretations consistent with the legislative purpose are available." *Griffin* v. *Oceanic Contractors, Inc.*, 458 U.S. 564, 575 (1982).

## II. Excluding Administrative Proceedings From The Six-Year Limitations Period Is Contrary To Section 2415's Origins And History

### A. Section 2415 Was Enacted To Address Administrative Processes

Section 2415's origins also belie the claim that it was designed to address only judicial claims. To the contrary, it was the potential abuse of *administrative* processes that led to Section 2415's enactment. As noted above, before 1966, there was no general statute of limitations governing actions brought by the United States against private parties seeking money under a contract. See Sen. Rep. No. 1328, *supra*, at 11-12. The need for a limitations period became evident during the 1965 hearings on the Comptroller General's government-contracts auditing procedures. See generally *Comptroller General Reports to Congress on Audits of*

*Defense Contracts: Hearings Before a Subcomm. of the H. Comm. on Gov't Ops.*, 89th Cong., 1st Sess. (1965) ("Defense Contractor Hearings"); Sen. Rep. No. 1328, *supra*, at 7 (citing the hearings). Those hearings addressed the Defense Department's and the General Accounting Office's use of two *administrative* procedures to recover money from government contractors: "voluntary refunds" and "unilateral" after-the-fact "price adjustments."[22]

Recognizing the unfairness of allowing such administrative recoveries decades after the fact, Representative Frank J. Horton asked "what statutes of limitations, if any, are applicable" to requests for voluntary refunds and use of the downward price adjustment procedure. Defense Contractor Hearings, *supra*, at 27. A Department of Defense lawyer responded that, "as far as administrative action is concerned," he did not believe the government "would be limited by any statute of limitations." *Id.* at 28. Representative Horton responded:

> It seems to me that the Government should have some sort of a burden placed on it so that it has to get in and examine this fairly soon after the contract is completed. And also that the contractor is entitled to know that he is at liberty at some point to at least go ahead and plan to utilize the profit that he has made

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[22] The "voluntary refund" procedure was "recommended" to agencies by the General Accounting Office. Defense Contractor Hearings, *supra*, at 7 (statement of Paul R. Ignatius, Ass't Sec'y of Defense). The "voluntary refund" procedure allowed an agency to request that a contractor repay a portion of the contract proceeds whenever the government determined, after the fact, that the contract price had included "'unnecessary,' 'excessive,' or 'unwarranted' costs." *Ibid.* The unilateral price adjustment procedure, provided in Section (e) of the Act of September 10, 1962, Pub. L. No. 87-653, 76 Stat. 528, codified as amended at 10 U.S.C. § 2306a(c), mandated that government contracts contain a clause requiring "the head of the agency" unilaterally to adjust the price of a contract downward if the agency determined that the contractor had "furnished cost or pricing data which * * * was inaccurate, incomplete, or noncurrent."

> and not have to keep on his books some sort of reserve to cover these contingencies.

*Ibid.*

The ensuing report of the Government Operations Committee declared that one "issue which demands corrective action * * * is the lack of a cutoff date for contractor liabilities." H.R. Rep. No. 1344, 89th Cong., 2d Sess. 16 (1966). The Committee observed that "contractors have no certainty that contracts 10 or 20 years old will not be subjected to renewed scrutiny or revision, with possible demands for refunds to the Government." *Ibid.* The Committee concluded "that there is general agreement that, in the interest of fairness, *a statute of limitations on matters related to audit and recoveries arising out of Government contracts* would be in order." *Ibid.* (emphasis added). The Committee recommended that the Department of Defense and the Department of Justice consult with the GAO and adopt recommendations for a statute of limitations "with the objective that a fair procedure be adopted and that contracts be closed out after a finite period." *Ibid.*

The Comptroller General and the Department of Justice ultimately responded by proposing H.R. 13652, which was enacted and then codified as Section 2415. The Senate Report explained that the bill "proposed that statutes of limitations be applied to important general areas where none are now in effect." Sen. Rep. No. 1328, *supra*, at 12. Specifically, the bill imposed "a 6-year limitation on the assertion of Government claims for money arising out of an express or implied contract or quasi-contract." *Ibid.*

Given that Section 2415 was proposed in response to potential abuses and delays in bringing administrative proceedings, it would be the height of irony to construe Section 2415 as exempting administrative proceedings from its scope. Surely a statute should not be read as inapplicable to the very abuses it was designed to correct. Each of the factors the House and Senate Reports cite in support of

Section 2415's enactment—fairness, ensuring the availability of evidence, and limiting record-keeping burdens, see pp. 4-5, *supra*—apply with as much force to administrative actions as to judicial actions. So too does the text of Section 2415 itself.

### B. The Exclusion Of Administrative Actions From Section 2415(a) Undermines Congress's Purpose In Establishing A Tolling Provision

Section 2415(a) undoubtedly restricts the time in which the government can file a lawsuit to six years. It also provides an exception where "administrative proceedings [are] required by contract or law." 28 U.S.C. § 2415(a). In that case, the government must bring suit "within one year after final decisions have been rendered" in the administrative proceedings. *Ibid.* The D.C. Circuit's interpretation would cause that exception to swallow the rule, effectively eliminating any limitations period even as to judicial actions: Any time administrative proceedings are *mandatory*, the government would have forever to begin those proceedings, *plus* a year from their completion to file a lawsuit. That result is directly contrary to the "elementary rule of construction that '[an] act cannot be held to destroy itself.'" *Citizens Bank of Md.* v. *Strumpf*, 516 U.S. 16, 20 (1995) (quoting *Tex. & Pac. R.R. Co.* v. *Abilene Cotton Oil Co.*, 204 U.S. 426, 446 (1907)).[23]

The legislative history is clear that, far from seeking to establish an infinite limitations period, Congress intended that exception to "toll[] the running of the statute of limitations during mandatory administrative proceedings." H.R. Rep. No. 1534, *supra*, at 4. Congress evidently understood that administrative proceedings would have to be brought within the six-year limitations period for tolling to occur. In general, to toll the limitations period for a judicial action, an administrative action must be initiated before the judicial

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[23] Here, the administrative proceedings invoked by MMS are not "required by contract or law," but rather are discretionary.

limitations period has lapsed. See, *e.g.*, *Webster* v. *Moore*, 199 F.3d 1256, 1259 (11th Cir. 2000) (holding that a state habeas petition that is filed following the expiration of AEDPA's limitations period cannot toll that period because "there is no period remaining to be tolled"). Consistent with that understanding, this Court has described the exception as "a one-year saving period to the government to overcome the effects of protracted administrative proceedings." *Crown Coat*, 386 U.S. at 521-522.

The D.C. Circuit's interpretation of Section 2415 would transform that tolling provision into a limitations period that does not begin to run until the government *chooses* to trigger it. If administrative actions are excluded from Section 2415, the government can wait any amount of time to bring an administrative action, and can delay filing suit until one year after voluntarily commencing that action and completing it. The six-year limitations period for bringing a court action is a virtual nullity if the government can evade it simply by opting to delay bringing an administrative action. This Court has long declined to "construe [a statute of limitations] as giving claimants an option as to when they will choose to start the period of limitation of an action." *McMahon* v. *United States*, 342 U.S. 25, 27 (1951). It should do likewise here.

### C. Later Amendments To Section 2415 Confirm That It Addresses Administrative Actions

Subsequent amendments to Section 2415 confirm that Congress intended it to address administrative actions. As enacted in 1966, Section 2415 provided that any claims accruing in the centuries that preceded its enactment would be deemed to accrue on the date of Section 2415's enactment. As the deadline for suit approached, however, Congress repeatedly found it necessary to extend the deadline for pre-1996 claims because the Indian tribes and the Department of the Interior could not identify and pursue the claims in time. See p. 6, *supra*. Those included a significant number of claims arising from "violations of lease agree-

ments," among others. *Time Extension For Commencing Actions on Behalf of Indians: Hearing before the Subcomm. on Indian Affairs of the S. Comm. on Interior and Insular Affairs*, 92d Cong., 2d Sess. 38 (1972) (joint statement of Arthur Lazarus, Jr., Martin J. Sonosky, and Charles A. Hobbs). If the court of appeals' holding were correct, the numerous extensions enacted by Congress would have been wholly unnecessary. Any claims could have been pursued administratively in perpetuity.

The D.C. Circuit's construction is likewise inconsistent with the system Congress eventually established. Under the Indian Claims Limitation Act, claims arising before Section 2415's enactment are not barred until a specified period after the Secretary of the Interior's publication of the claim, or publication of the Secretary's decision to reject the claim. See Indian Claims Limitation Act of 1982, § 2(a), 96 Stat. 1976, codified at 28 U.S.C. § 2415(a). When the Secretary published the lists, 48 Fed. Reg. 13,698 (March 31, 1983), 48 Fed. Reg. 51,204 (Nov. 7, 1983), they included claim after claim for "breach of contract," "unpaid lease rentals," "mineral[s]," "gravel/fill/minerals/oil/gas removed" —precisely the claims that, under the D.C. Circuit's theory, could be pursued administratively in perpetuity.

## III. The United States' Alternative Arguments Are Without Merit

In its response to the petition for a writ of certiorari (at 17), the government also urged that Section 2415 cannot bar MMS's effort to recover additional royalties because MMS's claim is not "founded upon a contract" and does not seek "money damages" within the meaning of 28 U.S.C. § 2415(a). The D.C. Circuit, however, did not address those arguments, and this Court ordinarily will not "decide in the first instance issues not decided below." *Nat'l Collegiate Athletic Ass'n* v. *Smith*, 525 U.S. 459, 470 (1999). In any event, the arguments are unpersuasive. MMS's demand for additional royalties is founded on the lease agreement,

which is a contract. And MMS's demand for past-due sums allegedly owed under the lease, together with interest, unquestionably constitutes a demand for "money damages."

### A. The Demand For Additional Royalties Allegedly Due Under The Lease Is Founded On Contract

There can be little doubt that the government's claimed right to additional royalties is "founded on contract" within the meaning of Section 2415(a). The MLA provides that "lands subject to disposition under this chapter which are known or believed to contain oil or gas deposits may be leased by the Secretary." 30 U.S.C. § 226(a). Exercising authority under that provision, the Secretary has entered into lease agreements with Amoco that set forth the rights and obligations of each party. See J.A. 10-23. As the Department of the Interior has elsewhere observed, "the rights of the government as lessor and the rights of the lessee are embodied in a lease. A lease is a contract * * * ." Memorandum from Frederick N. Ferguson, Ass't Solicitor, Dep't of the Interior, Division of Minerals, to Chief, Conservation Division, Geological Survey, at 1-2 (May 10, 1974); see also William A. Geshuny, Assoc. Solicitor, Indian Affairs, Off. of the Solicitor, to All Regional Solicitors, at 2 (Jan. 20, 1972) ("This provision [2415(a)] would cover situations where the government would seek monetary compensation rather than cancellation, rescission, or specific performance of a contract. We believe the term 'contract' could be fairly construed to include a lease.").

The lower courts have, without exception, reached the same conclusion—an oil and gas lease is a contract. See *OXY USA*, 268 F.3d at 1007 ("We have long recognized that oil and gas leases are contracts."); *Cont'l Oil Co.* v. *United States*, 184 F.2d 802, 817 (9th Cir. 1950) ("We then have a contract which in terms obligates the lessee to pay a stated percentage of the value of the production."); *United States* v. *Ohio Oil Co.*, 163 F.2d 633, 637 (10th Cir. 1947) (holding that a claim under an oil and gas lease "arises under a lease contract" and the "result depends upon the judicial con-

struction of that contract"); *United States* v. *Gen. Petroleum Corp. of Cal.*, 73 F. Supp. 225, 234 (S.D. Cal. 1947) ("Regardless of the type of lease Congress might authorize, a lease executed in accordance with what it has authorized becomes a private contractual matter and is to be interpreted according to the general rules of law respecting contracts between individuals."). Even the unpublished Fifth Circuit opinion on which the government relies for other purposes (Br. in Opp. 19) held that "orders issued by MMS seek monies due under a contract with the government." *Phillips Petroleum Co.* v. *Johnson*, No. 93-1377, 1994 WL 484506, at *2 (5th Cir. Sept. 7, 1994).

The fact that a statutory and regulatory scheme affects the calculation of royalty payments does not alter that conclusion. The legal source of the government's entitlement to a royalty payment from Amoco originates in the lease itself, not the statutes and regulations that govern lease terms and administration. See *Ohio Oil*, 163 F.2d at 637; *Cont'l Oil*, 184 F.2d at 807. Notably, where the terms of a lease are inconsistent with an MMS regulation, it is the language of the lease, rather than the regulation, that determines the government's royalty rights. See 30 C.F.R. § 202.100(b)(3); see also 58 Cong. Rec. 7643 (1919) ("In other words, when the terms of the lease have once been established by the lease itself, those terms cannot then be changed by the action of Congress until the expiration of the term of the lease itself.") (statement of Rep. Anderson).

### B. Actions For Allegedly Past-Due Payments And Interest Are Actions for Money Damages

The government likewise errs in asserting (Br. in Opp. 19) that MMS efforts to recover money allegedly owed under a lease do not seek "money damages" but rather seek something "analogous to *equitable* monetary relief." Br. in Opp. 18-19. The assertion is, as an initial matter, incorrect. It is well established that "[a] suit upon a contractual obligation to pay money at a fixed or ascertainable time is a suit to recover *damage* for its breach." *Royal Indem. Co.* v.

*United States*, 313 U.S. 289, 295-296 (1941) (emphasis added); see p. 49 & n. 24, *infra* (citing additional cases).

The government also asks the wrong question. When determining whether a claim seeks money damages, the issue is not whether the relief can be characterized as "legal" or "equitable." It is instead whether the relief represents substitute "compensation" for a past wrong or instead provides "specific relief." *Bowen* v. *Massachusetts*, 487 U.S. 879, 895 (1988). While "[m]oney damages are * * * the classic form of *legal* relief," *Mertens* v. *Hewitt Assocs.*, 508 U.S. 248, 255 (1993), this Court has held that even actions seeking equitable relief can "constitute[ ] a claim for 'money damages.'" *Dep't of the Army* v. *Blue Fox, Inc.*, 525 U.S. 255, 263 (1999). The government itself recognized as much in *Blue Fox*, urging that the "'line * * * is not between actions at law and suits in equity.'" U.S. Br. in No. 97-1642, *Blue Fox*, at 31 (quoting *Hubbard* v. *Administrator, EPA*, 982 F.2d 531, 539 (D.C. Cir. 1992) (Randolph, J., joined by R.B. Ginsburg, J., concurring)). "Nor," the government continued, does the distinction follow the line "between 'equitable' and 'legal' remedies," since "'[w]hat may qualify as an 'equitable remedy' * * * is not synonymous with specific relief.'" *Ibid.* (quoting *Hubbard*, *supra*, at 537).

The government now quotes *Bowen* v. *Massachusetts*, 487 U.S. at 893-894, for the proposition that "[t]he fact that a remedy may require one party to pay money to another is not a sufficient reason to characterize the relief as 'money damages.'" Br. in Opp. 18. But *Bowen* explains the distinction between the recovery of money as "damages" and the recovery of money as "specific relief":

> The term "money damages," * * * normally refers to a sum of money used as compensatory relief. Damages are given to the plaintiff to *substitute* for a suffered loss, whereas specific remedies "are not substitute remedies at all, but attempt to give the plaintiff the very thing to which he was entitled." D. Dobbs, *Handbook on the Law of Remedies* 135 (1973).

*Bowen*, 487 U.S. at 895 (quoting *Md. Dep't of Human Res.* v. *Dep't of Health & Human Servs.*, 763 F.2d 1441, 1446 (D.C. Cir. 1985)). Applying that distinction, *Bowen* held that "the provision of the Administrative Procedure Act that precludes actions seeking 'money damages' against federal agencies * * * does not bar a State from seeking specific relief to obtain money to which it claims entitlement under the federal Medicaid statute * * * ." *Great-West Life & Annuity Ins. Co.* v. *Knudson*, 534 U.S. 204, 212 (2002).

*Bowen*, however, does not support characterizing a demand for past-due money *under a contract* as specific relief rather than compensatory money damages. To the contrary, while *Bowen* applies to *statutory* obligations, this Court has held it inapplicable where, as here, the action involves "a *contractual* obligation to pay *past due* sums." *Great-West*, 534 U.S. at 212. That is consistent with the universal understanding that "[a] suit upon a contractual obligation to pay money at a fixed or ascertainable time is a suit to recover *damage* for its breach." *Royal Indem. Co.*, 313 U.S. at 295-296 (emphasis added). The law hardly could be clearer that "damages are always the default remedy for breach of contract." *United States* v. *Winstar Corp.*, 518 U.S. 839, 885 (1996). Treatise after treatise agrees.[24]

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[24] See R. Thompson, *et al.*, *Remedies: Damages, Equity and Restitution* § 2.02, at 71 (3d ed. 2002) ("In Anglo-American Law * * * money damages is the dominant remedy for breach of contract."); 24 *Williston on Contracts* § 64:1, at 7 (4th ed. 1990) ("The goal of compensating the promisee following a breach of contract * * * is, to the extent possible through an award of money damages * * * ."); 11 *Corbin on Contracts* § 55.1, at 4 (rev. ed. 2005) ("In the law of contract, the term 'damages' is used to mean compensation in money as a substitute for and the equivalent of the promised performance."); J. Murray, *Murray on Contracts* § 117, at 772-773 (4th ed. 2001) ("The usual remedy available to an aggrieved party when a breach of contract has occurred is an action for the recovery of compensation in the form of money damages to protect the expectation interest, *i.e.*, an award that will place the injured promisee in the same position he would have been in had the contract been performed.").

If there were any doubt that the government's claim here is for compensatory "money damages" rather than for "specific relief," it would be erased by the fact that the MMS order seeks prejudgment interest on top of allegedly past-due royalties. Pet. App. 154a. This Court has long "recognized the compensatory nature of prejudgment interest." *City of Milwaukee* v. *Cement Div., Nat'l Gypsum Co.*, 515 U.S. 189, 196 n.7 (1995); see also *Flint* v. *ABB, Inc.* 337 F.3d 1326, 1330 (11th Cir. 2003) ("[I]nterest on money past due under a contract is a classic form of *compensatory damages* and, as such, does not qualify as 'equitable relief.'") (emphasis added). Moreover, an interest payment that was not due at the time the obligation to pay was allegedly breached cannot be "the very thing to which [the government] was entitled" under the lease. *Bowen*, 487 U.S. at 895. It is instead part of the substitute payment that compensates for the payment obligation that was not fulfilled. As such, it is money damages, not "specific relief." See *Blue Fox*, 525 U.S. at 262-263.

## CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be reversed.

Respectfully submitted.

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## STATUTORY APPENDIX

Section 2 of the Act of July 18, 1966, 80 Stat. 304, codified as amended at 28 U.S.C. § 2415, *et seq.*, provides, in relevant part:

**§ 2415. Time for commencing actions brought by the United States**

(a) Subject to the provisions of section 2416 of this title, and except as otherwise provided by Congress, every action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later: *Provided*, That in the event of later partial payment or written acknowledgment of debt, the right of action shall be deemed to accrue again at the time of each such payment or acknowledgment: *Provided further*, That an action for money damages brought by the United States for or on behalf of a recognized tribe, band or group of American Indians shall not be barred unless the complaint is filed more than six years and ninety days after the right of action accrued: *Provided further*, That an action for money damages which accrued on the date of enactment of this Act in accordance with subsection (g) brought by the United States for or on behalf of a recognized tribe, band, or group of American Indians, or on behalf of an individual Indian whose land is held in trust or restricted status, shall not be barred unless the complaint is filed sixty days after the date of publication of the list required by section 4(c) of the Indian Claims Limitation Act of 1982: *Provided*, That, for those claims that are on either of the two lists published pursuant to the Indian Claims Limitation Act of 1982, any right of action shall be barred unless the complaint is filed

within (1) one year after the Secretary of the Interior has published in the Federal Register a notice rejecting such claim or (2) three years after the date the Secretary of the Interior has submitted legislation or legislative report to Congress to resolve such claim or more than two years after a final decision has been rendered in applicable administrative proceedings required by contract or by law, whichever is later.

**(b)** Subject to the provisions of section 2416 of this title, and except as otherwise provided by Congress, every action for money damages brought by the United States or an officer or agency thereof which is founded upon a tort shall be barred unless the complaint is filed within three years after the right of action first accrues: *Provided*, That an action to recover damages resulting from a trespass on lands of the United States; an action to recover damages resulting from fire to such lands; an action to recover for diversion of money paid under a grant program; and an action for conversion of property of the United States may be brought within six years after the right of action accrues, except that such actions for or on behalf of a recognized tribe, band or group of American Indians, including actions relating to allotted trust or restricted Indian lands, may be brought within six years and ninety days after the right of action accrues, except that such actions for or on behalf of a recognized tribe, band, or group of American Indians, including actions relating to allotted trust or restricted Indian lands, or on behalf of an individual Indian whose land is held in trust or restricted status which accrued on the date of enactment of this Act in accordance with subsection (g) may be brought on or before sixty days after the date of the publication of the list required by section 4(c) of the Indian Claims Limitation Act of 1982: *Provided*, That, for those claims that are on either of the two lists published pursuant to the Indian Claims Limitation Act of 1982, any right of action shall be barred unless the complaint is filed within (1)

one year after the Secretary of the Interior has published in the Federal Register a notice rejecting such claim or (2) three years after the Secretary of the Interior has submitted legislation or legislative report to Congress to resolve such claim.

(c) Nothing herein shall be deemed to limit the time for bringing an action to establish the title to, or right of possession of, real or personal property.

(d) Subject to the provisions of section 2416 of this title and except as otherwise provided by Congress, every action for the recovery of money erroneously paid to or on behalf of any civilian employee of any agency of the United States or to or on behalf of any member or dependent of any member of the uniformed services of the United States, incident to the employment or services of such employee or member, shall be barred unless the complaint is filed within six years after the right of action accrues: *Provided*, That in the event of later partial payment or written acknowledgment of debt, the right of action shall be deemed to accrue again at the time of each such payment or acknowledgment.

(e) In the event that any action to which this section applies is timely brought and is thereafter dismissed without prejudice, the action may be recommenced within one year after such dismissal, regardless of whether the action would otherwise then be barred by this section. In any action so recommenced the defendant shall not be barred from interposing any claim which would not have been barred in the original action.

(f) The provisions of this section shall not prevent the assertion, in an action against the United States or an officer or agency thereof, of any claim of the United States or an officer or agency thereof against an opposing party, a co-party, or a third party that arises out of the transaction or occurrence that is the subject matter of the opposing

party's claim. A claim of the United States or an officer or agency thereof that does not arise out of the transaction or occurrence that is the subject matter of the opposing party's claim may, if time-barred, be asserted only by way of offset any may be allowed in an amount not to exceed the amount of the opposing party's recovery.

(g) Any right of action subject to the provisions of this section which accrued prior to the date of enactment of this Act shall, for purposes of this section, be deemed to have accrued on the date of enactment of this Act.

(h) Nothing in this Act shall apply to actions brought under the Internal Revenue Code or incidental to the collection of taxes imposed by the United States.

(i) The provisions of this section shall not prevent the United States or an officer or agency thereof from collecting any claim of the United States by means of administrative offset, in accordance with section 3716 of title 31.

**§ 2416. Time for commencing actions brought by the United States—Exclusions**

For the purpose of computing the limitations periods established in section 2415, there shall be excluded all periods during which—

(a) the defendant or the res is outside the United States, its territories and possessions, the District of Columbia, or the Commonwealth of Puerto Rico; or

(b) the defendant is exempt from legal process because of infancy, mental incompetence, diplomatic immunity, or for any other reason; or

(c) facts material to the right of action are not known and reasonably could not be known by an official of the United States charged with the responsibility to act in the circumstances; or

(d) the United States is in a state of war declared pursuant to article I, section 8, of the Constitution of the United States.

SUPREME COURT, U.S.
FILED
MAR 13 2006
OFFICE OF THE CLERK

(2)

No. 05-669

# In the Supreme Court of the United States

BP AMERICA PRODUCTION COMPANY, SUCCESSOR IN INTEREST TO AMOCO PRODUCTION COMPANY, ET AL., PETITIONERS

*v.*

REJANE BURTON, ACTING ASSISTANT SECRETARY, LAND AND MINERALS MANAGEMENT, DEPARTMENT OF THE INTERIOR, ET AL.

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT*

## BRIEF FOR THE RESPONDENTS

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## QUESTIONS PRESENTED

1. Whether the Department of the Interior reasonably interpreted the Mineral Leasing Act of 1920, 30 U.S.C. 181 *et seq.*, and its longstanding regulations implementing that Act, to provide that the cost of removing excess carbon dioxide from coalbed methane produced in the San Juan Basin is not deductible from the value of production for royalty purposes.

2. Whether the six-year limitations period of 28 U.S.C. 2415(a) governs the issuance of administrative orders, as opposed to the government's filing of a complaint in court.

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# In the Supreme Court of the United States

No. 05-669

BP AMERICA PRODUCTION COMPANY, SUCCESSOR IN INTEREST TO AMOCO PRODUCTION COMPANY, ET AL., PETITIONERS

*v.*

REJANE BURTON, ACTING ASSISTANT SECRETARY, LAND AND MINERALS MANAGEMENT, DEPARTMENT OF THE INTERIOR, ET AL.

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT*

## BRIEF FOR THE RESPONDENTS

### OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-20a) is reported at 410 F.3d 722. The opinion of the district court (Pet. App. 21a-56a) is reported at 300 F. Supp. 2d 1.

### JURISDICTION

The judgment of the court of appeals was entered on June 10, 2005. A petition for rehearing was denied on August 24, 2005 (Pet. App. 175a). The petition for a writ of certiorari was filed on November 22, 2005. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

## STATEMENT

1. Congress enacted the Mineral Leasing Act of 1920 (MLA or the Act), 30 U.S.C. 181 *et seq.*, to promote prudent development of mineral resources on public lands and "to obtain for the public a reasonable financial return on assets that 'belong' to the public." *California Co.* v. *Udall*, 296 F.2d 384, 388 (D.C. Cir. 1961). Congress charged the Department of the Interior with collecting royalty payments from federal lessees, 30 U.S.C. 1711, who must pay royalties at the rate of at least 12.5 percent of the "amount or value of the production removed or sold from the lease." 30 U.S.C. 226(b)(1)(A).

The MLA directs the Department to "prescribe necessary and proper rules and regulations * * * to carry out" the leasing provisions. 30 U.S.C. 189. The Department's regulations provide that under no circumstances shall the value of production for royalty purposes be less than the "gross proceeds" accruing to the lessee. 30 C.F.R. 206.152(h). "Gross proceeds" is defined as "the total monies and other consideration accruing to * * * [a] gas lessee for the disposition of the gas." 30 C.F.R. 206.151.

Under the Department's regulations, the lessee must "place gas in marketable condition" "at no cost to the Federal Government." 30 C.F.R. 206.152(i). Further, the amount of gross proceeds is increased "to the extent that the gross proceeds have been reduced because the purchaser, or any other person, is providing certain services the cost of which ordinarily is the responsibility of the lessee to place the gas in marketable condition." *Ibid.* The regulations define products in "marketable condition" as being those that are "sufficiently free from impurities and otherwise in a condition that they will be

accepted by a purchaser under a sales contract typical for the field or area." 30 C.F.R. 206.151.

2. From 1989 until 1996, Amoco Production Company (Amoco), one of the predecessors in interest to petitioner BP America Production Company, extracted coalbed methane gas under various federal leases in the San Juan Basin in New Mexico. The extracted gas consisted of more than ten percent carbon dioxide ($CO_2$), which has no energy content and reduces the energy value of the gas. Pet. App. 70a.

Amoco sold most of the gas to purchasers who, at a location removed from the wellhead, treated the gas to reduce its $CO_2$ level. The treated gas was subsequently transported and marketed through a mainline transportation system to end users mainly in California. See Pet. App. 69a-72a. The $CO_2$ level had to be reduced to meet the specifications of the mainline transportation system, which would permit only one to three percent $CO_2$ content. *Id.* at 84a & n.18. Amoco also sold a small percentage of the gas at the wellhead to purchasers who used the gas without first treating it to reduce its $CO_2$ level. *Id.* at 74a-75a, 77a n.11.

For most of the relevant period, the purchaser of gas at the wellhead was a wholly owned affiliate of Amoco, the Amoco Energy Trading Company (AETC). The price that AETC paid Amoco, and on which Amoco based its royalty payments, was calculated as the amount AETC received from selling the gas to third parties, reduced by costs that AETC incurred to remove the excess $CO_2$ and transport the gas from the wellhead to the point where AETC sold it. Pet. App. 74a-75a.

Petitioner Atlantic Richfield Company and its subsidiary, Vastar Resources, Inc. (ARCO/Vastar), also extracted coalbed methane gas pursuant to various

leases on federal lands in the San Juan Basin in New Mexico. ARCO/Vastar sold its coalbed methane gas under arms-length sales arrangements. The price that ARCO/Vastar received under those arrangements was reduced by costs associated with treating the gas to remove excess $CO_2$. Pet. App. 99a-102a.

3. In 1996, the Interior Department's Minerals Management Service (MMS) responded to inquiries about how to calculate royalties on coalbed methane in the San Juan Basin by advising that a value derived from gross proceeds "cannot be reduced, either directly or indirectly, for the costs of placing coalbed methane in marketable condition. Placing production in marketable condition includes, but is not limited to, $CO_2$ removal." Pet. App. 170a.

Pursuant to the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. 1701 *et seq.*, the State of New Mexico performed an audit of Amoco's royalty calculations. Pet. App. 68a-69a; see 30 U.S.C. 1735. Based on that audit, MMS issued an order on May 27, 1997, directing Amoco to pay royalties of $4,117,607 for sampled leases and production months, and to perform a restructured accounting for all of its leases in the San Juan Basin producing coalbed methane for the period January 1989 through August 1996. Pet. App. 144a-145a.

MMS found that coalbed methane in the San Juan Basin generally has a high $CO_2$ content, as much as 12 to 15 percent, and that "to transport and sell the coalbed methane, the $CO_2$ level has to be reduced to around 2 or 3 percent." Pet. App. 145a. MMS determined that in calculating the value of production for royalty purposes, Amoco had improperly deducted various costs, including

$CO_2$ removal costs, contrary to the requirements of the marketable condition rule. *Id.* at 145a-148a.

The State of New Mexico also performed an audit of ARCO/Vastar's royalty calculations. Pet. App. 98a-99a. Based on that audit, MMS issued an order on January 22, 1997, directing ARCO/Vastar to pay royalties of $782,373 for sampled leases and production months and to perform a restructured accounting for all of its leases in the San Juan Basin producing coalbed methane for the period January 1989 through August 1996. *Id.* at 166a-167a. MMS determined that ARCO/Vastar, in its royalty calculations, had improperly deducted the costs of treating coalbed methane to meet mainline pipeline standards. *Id.* at 157a-169a.

Both petitioners took administrative appeals, which were denied in pertinent part by the Assistant Secretary for Land and Minerals Management. Pet. App. 68a-97a, 98a-126a. In each case, the Assistant Secretary determined that while there was evidence of sales of untreated coalbed methane at the wellhead for use in that area without further treatment, the demand for such sales was very limited, amounting to between 10 and 20 percent of the total San Juan Basin coalbed methane production. *Id.* at 62a-65a, 76a-78a & n.11, 81a-83a & n.17, 103a-105a. The remainder of the gas was sold for use in distant markets and had to be treated to reduce its $CO_2$ content for those uses and for transmission in the pipelines. *Id.* at 62a-65a, 76a-85a, 103a-105a.

The Assistant Secretary determined that because the limited demand for gas used in untreated form was not typical for gas produced from the field or area, Pet. App. 64a-65a, 77a, 105a-106a, "the value for royalty purposes" of the gas not consumed locally "must be determined by adding to the gross proceeds received from the wellhead

purchaser the cost of treating the gas for the removal of $CO_2$ to the level required to place the gas in marketable condition." *Id.* at 81a, 105a.

Relying on prior Interior Board of Land Appeals (IBLA) decisions, the Assistant Secretary also rejected Amoco's contention that the administrative proceedings were time-barred by 28 U.S.C. 2415, which imposes a six-year limitations period for the filing of a "complaint" in an "action for money damages" brought by the United States and founded upon a contract. Pet. App. 95a-96a. The Assistant Secretary explained that the limitations period does not apply to administrative appeals. *Id.* at 96a.

4. Petitioners sought review in the United States District Court for the District of Columbia, which rejected their challenges. Pet. App. 21a-56a. The court concluded that the Assistant Secretary had reasonably determined that "the gas at issue is not marketable unless it has reduced levels of $CO_2$." *Id.* at 39a. The court also ruled that the statute of limitations found in 28 U.S.C. 2415(a) does not apply to the agency's administrative orders. Pet. App. 48a-55a.

5. The court of appeals unanimously affirmed in a decision authored by then-Judge Roberts. Pet. App. 1a-20a. The court first rejected petitioners' argument that the MLA unambiguously requires MMS to calculate royalties based on the gross proceeds of sales made at the wellhead, as opposed to sales made at other locations. *Id.* at 7a-8a. The statute looks to the "amount or value of the production removed or sold from the lease," and the court concluded that "[t]he phrase 'from the lease' is sufficiently broad to be read as referring simply to the origin of the gas." *Id.* at 8a. "Gas that is 'from the lease' and that is marketed at a remote location can readily be

described as gas 'removed or sold from the lease.' The producers read the statute as if it referred to gas 'sold *at* the lease,' but that is not the case." *Ibid.* (quoting 30 U.S.C. 226(b)(1)(a)). Having found the statute ambiguous, the court of appeals upheld the Assistant Secretary's interpretation as reasonable because petitioners had presented no challenge to the reasonableness of that interpretation under *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-845 (1984), and instead had argued only that the statutory text was unambiguous. Pet. App. 8a-9a.

The court then held that the agency's decisions were consistent with its regulation defining gas in "marketable condition" to be gas acceptable to "a purchaser under a sales contract typical for the field or area." 30 C.F.R. 206.151; see Pet. App. 9a-11a. Although petitioners argued that untreated gas sold at the leasehold was in marketable condition under that regulation, the court of appeals deferred to the agency's contrary interpretation. The court noted both that the "field or area" was not necessarily limited to the specific leasehold, and that in any event the Assistant Secretary did not err in determining that "typical" sales contracts for the leases at issue were those that required removal of excess $CO_2$ for transportation to a distant location. *Id.* at 10a-11a.

Finally, the court of appeals held that the Department's orders were not time-barred by 28 U.S.C. 2415(a). Pet. App. 16a-20a. The court noted that the statute limits only the filing of a "complaint" in an "action for money damages," and "[t]he phrase 'action for money damages' points strongly to a suit in a court of law, rather than an agency enforcement order." *Id.* at 16a. "Any doubt is removed," in the court's view, "by the fact that subsection 2415(a) measures the limitations

period from the filing of a 'complaint,'" because the Department issued an "*order*," not a "complaint." *Id.* at 17a. In so holding, the court of appeals expressly agreed with a decision of the Fifth Circuit, *id.* at 20a (citing *Phillips Petroleum Co.* v. *Johnson*, No. 93-1377, 1994 WL 484506 (5th Cir. Sept. 7, 1994), cert. denied, 514 U.S. 1092 (1995)), but disagreed with decisions of the Tenth and Federal Circuits, *id.* at 18a (citing *OXY USA, Inc.* v. *Babbitt*, 268 F.3d 1001 (10th Cir. 2001) (en banc); *United States* v. *Hanover Ins. Co.*, 82 F.3d 1052 (Fed. Cir. 1996)).

## DISCUSSION

Petitioners' challenge to the specific methodology used to calculate royalty payments for coal bed methane leases in the San Juan Basin does not warrant further review. The decision of the court of appeals on that issue is correct and does not conflict with any decision of another court of appeals. The court of appeals' holding that the limitations period of 28 U.S.C. 2415(a) does not apply to administrative orders is also correct. The courts of appeals are divided on that question, however, and it is sufficiently important and recurring that review by this Court would be appropriate. Thus, this Court should grant the petition limited to the second question presented.

1. a. The MLA requires lessees to pay royalties "at a rate of not less than 12.5 percent in amount or value of the production removed or sold from the lease." 30 U.S.C. 226(b)(1)(A). Exercising its authority to administer the MLA and to "prescribe necessary and proper rules and regulations * * * to carry out" the leasing provisions, 30 U.S.C. 189, the Department has specified that the "value of production" for royalty purposes is

"under no circumstances" less than the "gross proceeds accruing to the lessee for lease production." 30 C.F.R. 206.152(h), 206.153(h). Further, the lessee must "place gas in marketable condition" "at no cost to the Federal Government." 30 C.F.R. 206.152(i).

Under the Department's regulations, products are in "marketable condition" if they are "sufficiently free from impurities and otherwise in a condition that they will be accepted by a purchaser under a sales contract typical for the field or area." 30 C.F.R. 206.151. In order to ensure that lessees do in fact bear the full cost of putting the product in marketable condition, the amount of "gross proceeds" for royalty purposes is increased "to the extent that the gross proceeds have been reduced because the purchaser, or any other person, is providing certain services the cost of which ordinarily is the responsibility of the lessee to place the gas in marketable condition." 30 C.F.R. 206.152(i).

For 45 years the courts have upheld the Department's "marketable condition" requirement as a reasonable interpretation of the Act, and petitioner does not appear to challenge that requirement here. See, *e.g.*, *California Co.* v. *Udall*, 296 F.2d 384, 387-388 (D.C. Cir. 1961); *Mesa Operating Ltd. P'ship* v. *Department of the Interior*, 931 F.2d 318, 325 (5th Cir. 1991), cert. denied, 502 U.S. 1058 (1992); cf. *Amerada Hess Corp.* v. *Department of Interior*, 170 F.3d 1032, 1036-1037 (10th Cir. 1999).

b. Although petitioners contend (Pet. 20-22) that the Department misapplied the "marketable condition" requirement in the circumstances of this case, the agency reasonably determined that petitioners' coalbed methane was not in marketable condition until excess $CO_2$ had been removed, and that the costs associated with

$CO_2$ removal therefore may not be deducted from gross proceeds for royalty purposes. Pet. App. 77a, 103a-105a.

The vast majority of the coalbed methane produced by petitioners was sold and used in distant markets and had to be conditioned for sale in those markets by removing excess $CO_2$. Pet. App. 77a-78a, 104a. Indeed, petitioners admitted below that most of the gas was consumed in California markets to which it was transported by pipelines that bought the gas from petitioners. Pet. C.A. Br. 31. Those pipelines treated and conditioned the gas to remove most of the $CO_2$ before putting it in their pipelines for transportation to California. Further, the price the pipelines (and in later periods, affiliated purchasers) paid for the gas was determined by adjusting for the costs of $CO_2$ removal. See Pet. App. 147a-153a.

Although a small percentage of the gas produced by petitioners in the San Juan Basin is sold and used in untreated form, gas is in marketable condition only if it is acceptable under a "typical" sales contract for the field or area. 30 C.F.R. 206.151. Here, the agency reasonably concluded that contracts for untreated gas were not typical for the field or area because only a limited amount of gas was sold and used in that manner. See Pet. App. 11a, 62a-65a, 103a-105a.[1]

c. Petitioners argue (Pet. 15-18) that the phrase "value of the production removed or sold from the lease" in 30 U.S.C. 226(b)(1)(A) unambiguously requires that gross proceeds always be calculated based on the condition in which some gas is sold and used at or near the wellhead, even if such sales comprise only a small percentage of the production. As the court of appeals rec-

[1] Further, all federal leases expressly provide that the Department has authority to establish the reasonable value of production for royalty purposes. See, *e.g.*, ARCO/Vastar A.R. 310.

ognized, however, the statutory text does not contain such a geographic limitation. Pet. App. 8a. Instead, "[t]he phrase 'from the lease' is sufficiently broad to be read as referring simply to the origin of the gas. Gas that is 'from the lease' and that is marketed at a remote location can readily be described as gas 'removed or sold from the lease.'" *Ibid.*

The statutory phrase "removed or sold from the lease" also prescribes a "trigger" for when a royalty obligation accrues—the time when production is "removed or sold from the lease." 30 U.S.C. 226(b)(1)(A). If a lessee extracts production but is able to store it at the lease, instead of selling or removing it from the lease, the royalty obligation does not accrue. See *BWAB Inc.*, 108 I.B.L.A. 250, 255-256 (1989).

Consequently, the court of appeals correctly held that Congress did not unambiguously require that the value of production always be measured according to the condition in which some gas is sold and used at or near the wellhead, as petitioners would have it. Instead, Congress conferred authority on the Department to determine how to calculate the value of production, see *California Co.*, 296 F.2d at 387, and the Department's reasonable interpretation of that ambiguous statutory provision is entitled to deference, see, *e.g.*, *Chevron U.S.A. Inc.* v. *Natural Res. Def. Council, Inc.*, 467 U.S. 837, 842-845 (1984).

Here, there is no dispute that the agency's interpretation is at least reasonable. As the court of appeals emphasized, petitioners did not dispute the reasonableness of the agency's interpretation before that court, and therefore waived any argument under *Chevron*'s second step. Pet. App. 8a-9a. In any event, the Department reasonably determined that the costs at issue are

non-deductible costs of putting the gas in marketable condition, as explained above. Contrary to petitioners' suggestion (Pet. 17), the agency's interpretation does not reach all so-called "downstream enhancements" in value. The marketable condition rule only requires petitioners to bear the cost of conditioning the gas for a purchaser under a contract typical for production from the field or area.

d. In addition to arguing that the Department ran afoul of the unambiguous text of the Act, petitioners contend (Pet. 18-23) that the agency's decision is a break from its past practice and inconsistent with its regulations. Petitioners cannot, however, cite any ruling that has limited the determination of marketable condition in all circumstances to sales and uses at the wellhead. See Pet. App. 11a-12a. Petitioners' claim that royalty calculations for coalbed methane produced in the San Juan Basin were always so limited is wrong. MMS accepted royalty payments from lessees "subject to audit" in accordance with its usual practice, Gov't C.A. Br. 42, and such "administrative acquiescence does not, therefore, rise to the level of long-standing policy." *Shoshone Indian Tribe* v. *Hodel*, 903 F.2d 784, 788 (10th Cir. 1990).

Nor is the agency's decision inconsistent with its regulation. The agency's interpretation of its own regulation is entitled to "controlling weight unless it is plainly erroneous or inconsistent with the regulation." *Thomas Jefferson Univ.* v. *Shalala*, 512 U.S. 504, 512 (1994) (quoting *Udall* v. *Tallman*, 380 U.S. 1, 16-17 (1965)); Pet. App. 9a. The regulatory definition of "marketable condition" looks to contracts that are "typical for the field or area." 30 C.F.R. 206.151. As the court of appeals held, that phrase does not "foreclose the possibility of defining a region beyond the geographical limits of

a leasehold." Pet. App. 10a. To the contrary, the Department's regulations expressly contemplate that the value of gas may be determined "at a point (e.g., sales point or point of value determination) *off the lease*," and then permit a deduction in such circumstances for costs of transporting the product but not of putting it in marketable condition. 30 C.F.R. 206.156(a) (emphasis added). Petitioners' contention (Pet. 19) that the location of the treatment should be dispositive is inherently arbitrary, because it would enable lessees to reduce their royalty payments merely by relocating their conditioning plants or arranging for others to do the conditioning at a different location.

Petitioners' heavy reliance (Pet. 4, 20-22) on the regulations governing *transportation* costs is misplaced because conditioning and transportation costs are different. While conditioning makes a product acceptable to buyers and therefore marketable, transportation moves that marketable product to the location where it will be sold. There is nothing inherently contradictory in concluding that the federal government should share the costs (by taking a reduced royalty) of transporting the product to the place where it will be sold, but not share the costs of putting the product in marketable condition. See *Independent Petroleum Ass'n of Am.* v. *DeWitt*, 279 F.3d 1036, 1041 (D.C. Cir. 2002), cert. denied, 537 U.S. 1105 (2003). Petitioners point to no provision of the MLA that requires the agency to treat the two categories of costs in the same way.[2]

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[2] Petitioners also accuse the agency (Pet. 16) of acting inconsistently with the history and practice of mineral leasing not involving the federal government. Even assuming *arguendo* that petitioners' historical analysis is accurate, this case is not governed by the variety of state laws but instead by an Act of Congress that the Department has

e. Petitioners err in contending (Pet. 17-20) that the courts of appeals are divided on this issue. Although petitioners cite primarily (Pet. 18-20) to another D.C. Circuit decision, *California Company*, the D.C. Circuit in that case *upheld* the agency's ruling that the lessee could not deduct from its gross proceeds the costs of conditioning gas by removing excess amounts of a substance in order to make it suitable for pipeline transmission. 296 F.2d at 386-388. Petitioners are correct (Pet. 20) that the gas there was conditioned near the wellhead, but as the court of appeals observed, that serves only to demonstrate that *California Company* did not address the issue presented here. Pet. App. 8a. Although petitioners also contend (Pet. 20) that *California Company* held that transportation costs should be excluded from the royalty base, that is an incorrect reading of *California Company*, which simply reserved the question. See 296 F.2d at 387. That contention is also irrelevant because in this case as in *California Company*, the agency has not sought to include transportation (as opposed to conditioning) costs in the royalty base. In any event, this Court does not sit to review alleged intra-circuit conflicts. *Wisniewski* v. *United States*, 353 U.S. 901, 902 (1957) (per curiam).

Nor are the other cases cited by petitioners in conflict with the decision below. *Continental Oil Co.* v. *United States*, 184 F.2d 802, 820 (9th Cir. 1950), considered whether gas volume lost through evaporation during transportation had to be included in the royalty calculation, not whether gas was in marketable condition. And in *Independent Petroleum Ass'n*, 279 F.3d at 1040, the D.C. Circuit *agreed* with the Department's determi-

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administered for more than 80 years.

nation that the costs of "downstream" marketing are not deductible from the royalty base.

2. Petitioners also challenge (Pet. 24-30) the court of appeals' holding that the limitations period of 28 U.S.C. 2415(a) does not apply to MMS's administrative orders to pay royalties. Although that holding is correct, the courts of appeals are divided on the question, which is an important and recurring one.[3]

a. Section 2415(a) does not bar MMS's order because it applies only to the filing of complaints in court, not to the issuance of administrative orders. That section states in pertinent part:

> [E]xcept as otherwise provided by Congress, every action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later.

28 U.S.C. 2415(a).

By its terms, Section 2415(a) applies only to an "action for money damages" initiated by a "complaint." 28 U.S.C. 2415(a). As the court of appeals recognized, those terms clearly connote judicial actions. Pet. App.

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[3] Although the limitations issue is properly presented by BP America as successor-in-interest to Amoco, ARCO/Vastar forfeited that claim by not raising it during the administrative proceedings or in the lower courts. See, *e.g.*, Pet. C.A. Br. 50-51 (raising this issue only with respect to Amoco); Pet. App. 48a (noting that Amoco made the argument). Thus, BP America is the only proper petitioner on this issue, and further proceedings on the issue could not affect the judgment as to ARCO/Vastar.

16a-17a (citing *Black's Law Dictionary* 285, 389 (6th ed. 1990)). Moreover, the "complaint" must be filed "within six years after the right of action accrues or within one year after final decisions have been rendered in applicable *administrative proceedings*, whichever is *later*." 28 U.S.C. 2415(a) (emphases added). Thus, the statute expressly distinguishes between administrative and judicial proceedings, with administrative proceedings *extending* the time bar for filing *in court*. In no way does the provision address, let alone limit, the time period for initiating administrative proceedings.

The statutory context and legislative history confirm the import of the plain text. Section 2415(a) is located within Title 28 of the United States Code, which is entitled "Judiciary and Judicial Procedure"—not administrative procedure—and in Title 28's Chapter 161, which governs the judiciary and judicial procedure in cases involving the "United States As Party Generally." The committee reports further confirm that "Section 2415 defines the time limitations for the United States to bring actions *in the U.S. courts*." H.R. Rep. No. 1534, 89th Cong., 2d Sess. 2 (1966) (emphasis added); S. Rep. No. 1328, 89th Cong., 2d Sess. 8 (1966) (emphasis added).

Although petitioners rely on Section 2415(i)'s exemption of administrative offsets from the six-year limitations period, that provision does not mean that administrative orders are generally subject to the statute of limitations. Courts construe statutory provisions not to be surplusage when "possible," *United States* v. *Menasche*, 348 U.S. 528, 538-539 (1955) (citation omitted), but the "preference for avoiding surplasage constructions is not absolute." *Lamie* v. *United States Tr.*, 540 U.S. 526, 536 (2004). Here, Section 2415(a) by its

plain terms does not apply to administrative orders, and its legislative history and placement in Title 28 confirm that it applies only to actions filed by the United States in court. As the court of appeals explained, the administrative-offset provision was added to the statute well after its enactment and for the purpose of resolving a specific disagreement regarding the treatment of offsets. Pet. App. 18a-19a; see S. Rep. No. 378, 97th Cong., 2d Sess. 16-17 (1982). Thus, the provision was designed to address a specific dispute by "clarifying" that the limitations period is inapplicable in the context of that dispute, *id.* at 2, not to reflect the view that administrative orders are generally subject to the statute of limitations.

Moreover, "[s]tatutes of limitation sought to be applied to bar rights of the Government, must receive a strict construction in favor of the Government." *Badaracco* v. *Commissioner*, 464 U.S. 386, 391 (1984) (quoting *E.I. DuPont de Nemours & Co.* v. *Davis*, 264 U.S. 456, 462 (1924)). As the court of appeals emphasized, "[e]xpanding the apparent scope of a statute of limitations beyond its plain language by inference from an express exception is hardly strict construction." Pet. App. 19a.

b. Even if the statute of limitations applied in some administrative contexts, it would not apply to orders to pay royalties under the MLA. The limitations period applies only to actions for "money damages" "founded upon [a] contract," and only if Congress has not "otherwise provided." 28 U.S.C. 2415(a).

The mineral leasing statutes and their implementing regulations create a comprehensive regulatory structure for the administration of leases. Lessees are initially responsible for computing and paying royalties. The Department, however, retains ultimate authority to de-

termine the value of the production on which royalties are based. See 30 U.S.C. 1711. If an audit reveals a possible underpayment, and MMS determines that additional royalties are in fact due, the agency issues an order to pay. That order is administratively appealable, and the Department's final decision, rendered by the IBLA or an Assistant Secretary, is subject to judicial review. See 30 C.F.R. Pt. 290; 43 C.F.R. Pt. 4.

If a lessee fails to make a required payment, the Department has a variety of remedies, only one of which involves seeking judicial enforcement of the order. See, *e.g.*, 30 U.S.C. 1719(c)(1), (e) (providing for administrative imposition of civil penalties for "knowingly or willfully fail[ing] to make any royalty payment by the date as specified by * * * order"); 30 U.S.C. 1719, 1720 (other civil and criminal penalties); 30 U.S.C. 1722(a) (authorizing civil action to "restrain any violation" or to "compel the taking of any action required"). The Department is unaware of any judicial action first brought by the government for collection or enforcement of a royalty claim.

In the context of that regulatory scheme, MMS's orders do not seek the payment of "money damages" within the meaning of 28 U.S.C. 2415(a). As this Court has explained, the fact that a remedy "may require one party to pay money to another is not a sufficient reason to characterize the relief as 'money damages.'" *Bowen* v. *Massachusetts*, 487 U.S. 879, 893-894 (1988) (citation omitted). Here, the administrative orders do not seek payment of "a sum of money used as compensatory relief," but instead compel lessees "to belatedly pay expenses that [they] should have paid all along." *Id.* at 894, 895 (citation omitted). Thus, the orders are more

analogous to *equitable* monetary relief than to *damages*. See *id.* at 894-896.

Nor are the orders to pay royalties "founded upon [a] contract" within the meaning of Section 2415(a). Instead, such orders are founded upon statutory and regulatory requirements. The incorporation of those requirements in leases does not change their fundamentally statutory and regulatory character for purposes of Section 2415(a), as shown by petitioners' exclusive reliance on the governing statutes and regulations. Cf. *Transohio Sav. Bank* v. *Director, Office of Thrift Supervision*, 967 F.2d 598, 609-610 (D.C. Cir. 1992).

c. Although the decision below is correct, there is a clear division among the courts of appeals. See Pet. App. 18a, 20a. The decision below agrees with a Fifth Circuit decision holding that orders to pay royalties under the MLA are not subject to the limitations period of Section 2415(a). See *Phillips Petroleum Co.* v. *Johnson*, No. 93-1377, 1994 WL 484506 (5th Cir. Sept. 7, 1994), cert. denied, 514 U.S. 1092 (1995); Pet. App. 20a. Although *Phillips Petroleum* is unpublished, it has precedential effect under Fifth Circuit Rule 47.5.3.

In conflict with those decisions, the en banc Tenth Circuit has squarely held that "the six-year statute of limitations provided by 28 U.S.C. § 2415(a) govern[s] [administrative] orders directing oil and gas lessees to pay additional royalties." *OXY USA, Inc.* v. *Babbitt*, 268 F.3d 1001, 1003 (2001). A divided panel of the Federal Circuit has similarly held, in tension with the decision below, that the Customs Service "cannot avoid the statute of limitations [of Section 2415(a)] by threat of administrative action based exclusively on non-payment of [a] time-barred claim" because "Congress has considered and dealt not only with judicial actions in section 2415,

but with extra-judicial agency actions as well." *United States* v. *Hanover Ins. Co.*, 82 F.3d 1052, 1055 (1996); but see *id.* at 1056-1057 (Bryson, J., dissenting).[4]

d. The issue has sufficient prospective importance to warrant this Court's review. In 1996, Congress enacted a seven-year limitations period for both judicial and administrative actions seeking the payment of obligations under federal oil and gas leases. 30 U.S.C. 1724(b)(1). Although that provision will likely prevent the question presented here from recurring in the context of oil and gas leases on federal lands, Section 1724(b)(1) does not apply to leases on Indian lands. See Federal Oil and Gas Royalty Simplification and Fairness Act of 1996, Pub. L. No. 104-185, § 9, 110 Stat. 1717 ("The amendments made by this Act shall not apply with respect to Indian lands."). Instead, it applies by its terms only to proceedings or demands based on an "obligation," 30 U.S.C. 1724(b)(1), a term which includes royalties for leases on federal but not Indian lands, 30 U.S.C. 1712.

The federal government also administers leases for minerals other than oil and gas, such as coal, other solid minerals, and geothermal resources. See 25 U.S.C. 396; 30 U.S.C. 181 *et seq.*; 30 U.S.C. 261 *et seq.*; 30 U.S.C. 1001 *et seq.* The seven-year limitations period for royalty obligations does not apply to those leases either, because the definition of "obligation" includes only oil and gas royalties. 30 U.S.C. 1712.

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[4] Petitioners also contend (Pet. 26) that the decision in *United States* v. *Suntip Co.*, 82 F.3d 1468 (9th Cir. 1996), cert. denied, 519 U.S. 1108 (1997), conflicts with the decision below. In *Suntip*, however, the Ninth Circuit applied 28 U.S.C. 2415(a) to a *judicial* action by the United States to enforce an administrative decision, and held that the limitations period begins to run upon entry of the administrative decision. 82 F.3d at 1475.

The upshot is that whether 28 U.S.C. 2415(a) applies to royalties not affected by 30 U.S.C. 1724(b)(1) will continue to arise in the context of Indian leases of all minerals and federal leases of minerals other than oil and gas. For fiscal year 2005, the Department reports that 27,817 leases of mineral and geothermal resources generated more than $8.7 billion in royalties. See Minerals Revenue Management, United States Dep't of the Interior <http://www.mrm.mms.gov/MRMWebStats/default.aspx>. Of those leases, 4456 covered either Indian lands or minerals other than oil and gas and generated over $1 billion in royalties.

Although the amount of royalty payments that are potentially subject to Section 2415(a)'s limitations period represents a relatively small portion of the total universe of royalty payments, the limitations issue is important in a significant number of cases. The Department estimates, for example, that more than 20 administrative appeals are currently pending from orders to pay royalties on Indian leases that likely implicate the limitations question at issue here. Moreover, the limitations period applies to actions brought by the United States generally, not only by the Department under the MLA. Although the issue appears to have arisen primarily in the context of orders to pay royalties under the MLA, it has arisen in other contexts, as the Federal Circuit's *Hanover Insurance* decision reflects.

For these reasons, this Court should grant review to resolve the circuit conflict on whether 28 U.S.C. 2415(a) applies in administrative proceedings.

## CONCLUSION

The petition for a writ of certiorari should be granted limited to the second question presented.

Respectfully submitted.

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No. 05-669

# In the Supreme Court of the United States

BP AMERICA PRODUCTION COMPANY, SUCCESSOR IN INTEREST TO AMOCO PRODUCTION COMPANY, ET AL., PETITIONERS

*v.*

REJANE BURTON, ACTING ASSISTANT SECRETARY, LAND AND MINERALS MANAGEMENT, DEPARTMENT OF THE INTERIOR, ET AL.

*ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT*

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## QUESTION PRESENTED

Whether the six-year limitations period of 28 U.S.C. 2415(a), which applies to the filing of a "complaint" in an "action for money damages" founded upon a contract, governs the issuance of administrative orders.

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# In the Supreme Court of the United States

No. 05-669

BP AMERICA PRODUCTION COMPANY, SUCCESSOR IN INTEREST TO AMOCO PRODUCTION COMPANY, ET AL., PETITIONERS

*v.*

REJANE BURTON, ACTING ASSISTANT SECRETARY, LAND AND MINERALS MANAGEMENT, DEPARTMENT OF THE INTERIOR, ET AL.

*ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT*

## BRIEF FOR THE RESPONDENTS

### OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-20a) is reported at 410 F.3d 722. The opinion of the district court (Pet. App. 21a-56a) is reported at 300 F. Supp. 2d 1.

### JURISDICTION

The judgment of the court of appeals was entered on June 10, 2005. A petition for rehearing was denied on August 24, 2005 (Pet. App. 175a). The petition for a writ of certiorari was filed on November 22, 2005, and was

granted limited to Question 2 on April 17, 2006. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

## STATEMENT

1. a. The Mineral Leasing Act of 1920 (MLA or the Act), 30 U.S.C. 181 *et seq.*, and other statutes charge the Secretary of the Interior with leasing federal and Indian lands for development of oil and gas resources. 30 U.S.C. 226(a); 25 U.S.C. 396, 396a-396g. By statute, lessees must pay royalties of at least 12.5% of the "amount or value of the production removed or sold from the lease." 30 U.S.C. 226(b)(1)(A). The Secretary interprets and implements that standard pursuant to his authority "to prescribe necessary and proper rules and regulations and to do any and all things necessary to carry out" the leasing program, 30 U.S.C. 189, including the issuance of administrative orders, see pp. 3-4, *infra*. Royalties from onshore federal oil and gas leases are generally divided evenly between the federal government and the State in which the leased land is located. 30 U.S.C. 191(a). Indian lessors, as landowners, receive all of the royalties derived from minerals extracted from their lands.

In 1982, Congress determined that because "the system of accounting with respect to royalties and other payments due and owing on oil and gas produced from * * * lease sites [was] archaic and inadequate," it was "essential that the Secretary initiate procedures to improve methods of accounting for such royalties and payments." 30 U.S.C. 1701(a)(2) and (3). In the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. 1701 *et seq.*, Congress therefore directed the Secretary to establish a comprehensive accounting, auditing, and collection system, 30 U.S.C. 1711(a), and to

"audit and reconcile, to the extent practicable, all current and past lease accounts for leases of oil or gas and [to] take appropriate actions to make additional collections or refunds as warranted." 30 U.S.C. 1711(c)(1). The Secretary delegated those responsibilities to the Minerals Management Service (MMS). See 30 C.F.R. 201.100.

Although lessees bear initial responsibility for calculating and paying royalties, MMS retains the right to audit a lessee's payments. 30 U.S.C. 1711; 30 C.F.R. 206.150(c), 206.170(d). MMS may also delegate that authority to the affected State or Indian Tribe. 30 U.S.C. 1732, 1735. If an audit reveals an apparent underpayment, MMS (or the affected State or Tribe on MMS's behalf) typically sends the lessee an issue letter that identifies the perceived deficiency and affords the lessee an opportunity to respond. See *Phillips Petroleum Co.* v. *Lujan*, 963 F.2d 1380, 1386 (10th Cir. 1992); *In re Amoco Prod. Co.*, 123 I.B.L.A. 278, 292 (1992) (Hughes, J., concurring). After reviewing any response, MMS determines whether there was an underpayment, and if so, it issues an order to pay additional royalties. See *ibid.* Such an order typically directs the payment of a specific amount of money, but if the lessee committed a systematic accounting error, it may also require the lessee to undertake a restructured accounting and to make an additional payment based on the result of that new accounting. See 30 U.S.C. 1724(d)(4); *Union Tex. Petroleum Energy Corp.*, 153 I.B.L.A. 170, 179 (2000). The Department's orders and decisions may also address compliance with requirements other than the payment of royalties, such as permits, easements, and rights of way, cooperative plans for oil and gas fields developed by more than one company, conservation of natural re-

sources, health and safety of workers, and discrimination. See, *e.g.*, 30 U.S.C. 185, 186, 225, 226(m); J.A. 12, 15, 17.

Administrative appeals of royalty orders are heard first by the Director of MMS or the Deputy Commissioner of Indian Affairs, 30 C.F.R. 290.105, and then (if further review is sought) by the Interior Board of Land Appeals (IBLA) or an Assistant Secretary, see 30 C.F.R. 290.108. Filing an appeal does not stay the order, 30 C.F.R. 218.50(c), but MMS will suspend the effect of an appealed order if the lessee complies with applicable bonding requirements or demonstrates financial solvency, 30 C.F.R. 243.8. Similar provisions apply to administrative appeals of other orders and decisions. See, *e.g.*, 30 C.F.R. 290.1 *et seq.*

If a lessee knowingly fails to comply with an order to pay, MMS may administratively assess civil penalties of up to $10,000 for each day a violation continues. 30 U.S.C. 1719(c). The Attorney General is also authorized to file an enforcement action in federal district court under 30 U.S.C. 1722(a), which authorizes the courts to "restrain any violation" of FOGRMA or to "compel the taking of any action required" under any federal mineral leasing law. Failure to comply with some types of MMS orders can also give rise to criminal liability. 30 U.S.C. 1720.

b. MMS has long maintained that the six-year statute of limitations of 28 U.S.C. 2415(a), which governs the filing of a "complaint" in an "action for money damages" "founded upon * * * contract," does not apply to the agency's administrative proceedings. *E.g.*, *Shell Oil Co.*, 150 I.B.L.A. 298, 306 (1999). In 1996, Congress enacted a seven-year limitations period for administrative orders and judicial proceedings arising from lessees' failure to

pay royalties for oil and gas leases on federal lands, and it clarified that Section 2415(a) does not apply to such orders and proceedings. Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 (FOGRSFA), Pub. L. No. 104-185, § 4(a), 110 Stat. 1704 (30 U.S.C. 1724(b)(1) and (3)). But the 1996 legislation does not apply to mineral leases on Indian lands, to federal leases for the development of minerals other than oil and gas (such as coal, other solid minerals, and geothermal resources), or to oil and gas production on federal leases before its enactment. FOGRSFA §§ 9, 11, 110 Stat. 1717 (30 U.S.C. 1701 note).

2. a. From 1989 to 1996, Amoco Production Company (Amoco), one of the predecessors in interest to petitioner BP America Production Company, extracted coalbed methane gas under various federal leases in the San Juan Basin in New Mexico. Pet. App. 68a-70a. Under the MLA, Amoco was required to pay royalties in the amount of 12.5% of the "amount or value of the production removed or sold from the lease." 30 U.S.C. 226(b)(1)(A); see J.A. 23 (reiterating that standard in one of petitioners' lease agreements).[1] The Interior Department's regulations have long defined the "value of production" to be the "gross proceeds" accruing to the lessee, 30 C.F.R. 206.152(h), and have prohibited lessees from deducting from their gross proceeds the costs of placing gas in marketable condition, 30 C.F.R. 206.152(i).

When the State of New Mexico conducted an audit of Amoco's royalty calculations, it determined that Amoco had not included in its gross proceeds the cost of condi-

[1] Although petitioners have a number of affected leases, only one of the lease agreements is in the record. See J.A. 10-23. The issues before this Court do not, however, turn on the terms of individual leases.

tioning gas for market by removing excess carbon dioxide ($CO_2$), which has no energy content and reduces the value of the gas. Pet. App. 144a-145a. After the State sent letters to Amoco concerning that matter during the summer of 1996, Amoco responded with a letter on October 15, 1996, that argued that removal of excess $CO_2$ should not be considered a cost of placing the gas in marketable condition. *Id.* at 150a.

Based on the State's audit and Amoco's response, MMS issued an order to pay on May 27, 1997. Pet. App. 144a-156a. MMS determined that Amoco had erred by excluding the costs of removing excess $CO_2$ from its gross proceeds, *id.* at 145a-148a, and ordered Amoco to pay additional royalties of $4,117,607 for the leases and years audited by the State, *id.* at 144a-145a, 153a. Because the audit uncovered a "consistent and systematic error" in Amoco's accounting, MMS also ordered Amoco to perform a restructured accounting for all of its leases in the San Juan Basin producing coalbed methane for the period January 1989 through August 1996. *Id.* at 153a. The order informed Amoco that failure to comply with its terms could give rise to civil penalties, *id.* at 154a, but that if Amoco timely pursued an administrative appeal, "compliance with [the] order will be suspended upon the posting of an adequate surety pending the outcome of the appeal," *id.* at 155a.

The Assistant Secretary of the Interior for Land and Minerals Management denied Amoco's administrative appeal. Pet. App. 68a-97a. The Assistant Secretary agreed with MMS that gas produced in the San Juan Basin was not in marketable condition until excess $CO_2$ was removed. *Id.* at 81a. Relying on prior IBLA decisions, the Assistant Secretary also rejected Amoco's contention that the six-year limitations period of 28

U.S.C. 2415 applies to administrative proceedings. Pet. App. 95a-96a.

b. Like Amoco, petitioner Atlantic Richfield Company and its subsidiary, Vastar Resources, Inc. (ARCO/Vastar), extracted coalbed methane gas pursuant to various leases on federal lands in the San Juan Basin. Pet. App. 4a. After an audit revealed that ARCO/Vastar had not included $CO_2$ removal costs in its gross proceeds, MMS issued an order to pay, and the Assistant Secretary denied ARCO/Vastar's appeal. *Id.* at 157a-174a; *id.* at 98a-126a. ARCO/Vastar did not, however, raise a statute-of-limitations defense before the agency.

3. Petitioners sought judicial review of the agency's final decisions in the United States District Court for the District of Columbia, which rejected their challenges. Pet. App. 21a-56a. After concluding that the Assistant Secretary had reasonably determined that "the gas at issue is not marketable unless it has reduced levels of $CO_2$," *id.* at 39a, the court rejected Amoco's contention that Section 2415(a) bars MMS from collecting royalties due more than six years before the agency issued the order to pay, *id.* at 48a-55a. The court explained that the statutory terms "action" and "complaint" "indicate[] that the statute applies to judicial proceedings, not administrative orders." *Id.* at 55a.

4. The court of appeals affirmed. Pet. App. 1a-20a. The court upheld the Assistant Secretary's decision on the merits, deferring to her interpretation of the MLA and the governing regulations. *Id.* at 7a-14a. The court also held that MMS's orders were not time-barred by 28 U.S.C. 2415(a). Pet. App. 16a-20a. Noting that the statute limits only the filing of a "complaint" in an "action for money damages," the court explained that "[t]he phrase 'action for money damages' points strongly to a

suit in a court of law, rather than an agency enforcement order that happens to concern money due under a statutory scheme." *Id.* at 16a. "Any doubt is removed," in the court's view, "by the fact that subsection 2415(a) measures the limitations period from the filing of a 'complaint,'" because MMS did not issue a "complaint" requesting relief, but instead issued "an *order*, the defiance of which incurs a 'Notice of Noncompliance' and subsequent civil penalties, absent a successful appeal." *Id.* at 17a.

The court of appeals noted that another provision in Section 2415 expressly exempts administrative offsets from the limitations period. Pet. App. 17a-18a (citing 28 U.S.C. 2415(i)). The court explained, however, that the administrative-offset provision was added to Section 2415 more than 16 years after its enactment to address a specific controversy regarding the treatment of offsets, and thus should not be read to mean—contrary to Section 2415(a)'s plain text—that the limitations period generally applies to administrative proceedings. *Id.* at 17a-19a. "[B]uttressing" that conclusion, in the court's view, is the canon of construction that "statutes of limitations against the sovereign are to be strictly construed." *Id.* at 19a. Finally, the court rejected Amoco's reliance on "the underlying purpose of repose animating section 2415" because "such appeals to purpose cannot override a statute's clear language." *Id.* at 19a-20a.

Because the court of appeals agreed with the government that an order directing the payment of royalties is not an action for money damages initiated by the filing of a complaint, it did not reach the government's alternative arguments that the order did not seek money damages and was not founded upon a contract within the meaning of Section 2415(a). Pet. App. 20a.

## SUMMARY OF ARGUMENT

Section 2415(a)—which must be strictly construed in favor of the government—applies only to the filing of a complaint in court, not to the issuance of an order by an administrative agency.

A. The statute governs the filing of a "complaint" in an "action for money damages." 28 U.S.C. 2415(a). At the time of Section 2415(a)'s enactment, the term "action" was ordinarily understood to mean "[t]he legal and formal demand of one's right from another person or party made and insisted on in a court of justice." *Black's Law Dictionary* 49 (4th ed. 1951). The ordinary meaning of the term "complaint" likewise referred to the pleading commencing a suit in court. Thus, commencing an "action" by filing a "complaint" refers, in its "ordinary sense," to filing a complaint in court, not to initiating an administrative proceeding. *Unexcelled Chem. Corp.* v. *United States*, 345 U.S. 59, 66 (1953). Section 2415(a) confirms that point by providing that the time to file a "complaint" in an "action" expires no sooner than one year after the final decision in applicable "administrative proceedings." 28 U.S.C. 2415(a). The statute thereby distinguishes between an "action" and an "administrative proceeding[]," with administrative proceedings triggering the time bar, not being limited by it.

Even if Section 2415(a) governed the initiation of some administrative proceedings, it would not apply to MMS's issuance of orders to pay, because orders are not complaints. Complaints seek relief; orders impose it. Although petitioners contend that an order to pay is functionally a complaint, it is not. Issued after an audit and informal agency process, an MMS order is legally binding on a lessee who has participated in the adminis-

trative scheme, unless the lessee both initiates a successful appeal and obtains a suspension of the order pending appeal by posting an adequate bond or demonstrating financial solvency.

B. The statutory context confirms Section 2415's plain meaning. Congress included Section 2415 in Title 28 of the United States Code, which is entitled "Judiciary and Judicial Procedure"—not administrative procedure—and in Title 28's Chapter 161, which governs the judiciary and judicial procedure in cases involving the "United States As Party Generally." Every other provision in Chapter 161 applies only to procedures in court, not to administrative proceedings. Like Section 2415(a), several of those provisions also use the term "action" to describe their applicability to suits in court.

C. The legislative history leaves little doubt that Section 2415(a) "defines the time limitations for the United States to bring *actions in the U.S. courts*." H.R. Rep. No. 1534, 89th Cong., 2d Sess. 2 (1966) (emphasis added). While the committee reports are saturated with references to the courts, they mention administrative proceedings only in discussing their effect on the time limit for filing a suit in court.

Petitioners' reliance on subsequent amendments to Section 2415(a) is misplaced. When it expressly excluded administrative offsets from the statute of limitations, Congress confirmed that it was only "clarifying" the statute on that point in light of a specific disagreement that had arisen about the treatment of offsets (but not about other administrative proceedings). S. Rep. No. 378, 97th Cong., 2d Sess. 2 (1982). Clarifying that the statute does *not* apply to one type of administrative proceeding hardly expresses an intent that it should apply to others. In any event, any such inference from

an amendment 16 years after Section 2415 was enacted would not be a basis for disregarding the statute's text, context, and the legislative history of the enactment of Section 2415 itself in 1966. If Section 2415 applied only to judicial proceedings before 1982, no rational Congress would have thought that the way to take the significant step of extending it to a multitude of administrative schemes would be a single reference to administrative offsets. The legislative history of amendments extending Section 2415's limitations period for some Indian claims, like the legislative history of the original Section 2415, similarly lends no support to petitioners' position because it confirms that Congress was concerned with suits in court, not administrative proceedings.

D. Petitioners' appeal to policy concerns cannot overcome Section 2415's clear text, context, and history. Moreover, there is little reason to assume that Congress would want the same across-the-board limitations period that governs suits in court to apply generally to the whole range of administrative proceedings. There are substantial differences between court and agency proceedings, and agency proceedings themselves differ from program to program. It would make especially little sense to apply Section 2415(a)'s limitations period for *initiating* court proceedings to MMS's *orders*, because MMS issues those orders after informal process. When Congress enacted a prospective limitations period for some orders to pay royalties, it therefore chose a longer period of seven, not six, years.

In addition, Congress enacted FOGRMA in 1982 because oil and gas lessees were underpaying royalties by staggering amounts—up to half a billion dollars annually. By instructing MMS to "audit and reconcile, to the extent practicable, all current *and past* lease accounts,"

Congress manifested an intent to promote recovery over repose. 30 U.S.C. 1711(c)(1) (emphasis added). Because it is not practical to audit all accounts, however, underpayments are difficult to identify and may go undetected for more than six years. That makes it all the more important to recover past underpayments when an audit reveals them, especially for Indian lessors to whom the government owes a trust responsibility.

## ARGUMENT

### THE LIMITATIONS PERIOD OF 28 U.S.C. 2415(a) DOES NOT GOVERN THE ISSUANCE OF ADMINISTRATIVE ORDERS

The court of appeals correctly held that the six-year limitations period of 28 U.S.C. 2415(a) applies only to the filing of a complaint in court, not to the issuance of an order by an administrative agency. That statute provides:

> [E]xcept as otherwise provided by Congress, every action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later.

28 U.S.C. 2415(a).

Congress enacted Section 2415(a) against the backdrop of two important canons of construction. First, "statutes of limitations against the sovereign are to be strictly construed," Pet. App. 19a, and the government "is subject to no time limitation, in the absence of con-

gressional enactment clearly imposing it." *E.I. DuPont de Nemours & Co.* v. *Davis*, 264 U.S. 456, 462 (1924); accord *Badaracco* v. *Commissioner*, 464 U.S. 386, 391 (1984). That principle reflects the more general rule that "limitations and conditions upon which the Government consents to be sued must be strictly observed and exceptions thereto are not to be implied." *Lehman* v. *Nakshian*, 453 U.S. 156, 161 (1981).

Second, a statute of limitations extinguishes only the remedy, not the underlying right. *Beach* v. *Ocwen Fed. Bank*, 523 U.S. 410, 416-417 (1998); *Semtek Int'l Inc.* v. *Lockheed Martin Corp.*, 531 U.S. 497, 504 (2001). Thus, a statute of limitations applicable to the government affects only those remedies the statute bars in terms clear enough to satisfy the strict-construction canon. *United States* v. *Whited & Wheless, Ltd.*, 246 U.S. 552, 561 (1918).

The text, context, and legislative history of Section 2415(a) demonstrate that it applies only to the filing of complaints in courts, not to the issuance of orders by agencies. Thus, "[t]he limitation set forth in section 2415(a) does not terminate all of the government's rights on a contract claim after six years, but merely eliminates one potential remedy—the filing of a lawsuit seeking money damages." *Thomas* v. *Bennett*, 856 F.2d 1165, 1169 (8th Cir. 1988).[2]

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[2] Although the limitations issue is properly presented by BP America as successor-in-interest to Amoco, ARCO/Vastar forfeited that claim by not raising it during the administrative proceedings or in the lower courts. See, *e.g.*, Pet. C.A. Br. 50-51 (raising this issue only with respect to Amoco); Pet. App. 48a (noting that Amoco made the argument). Thus, BP America is the only proper petitioner on this issue, and this Court's decision could not affect the judgment as to ARCO/Vastar. Gov't Pet.-stage Br. 15 n.3.

### A. The Ordinary Meanings of the Statutory Terms, Including "Action" and "Complaint," Refer to a Suit in Court

Because the statute does not define its terms, such as "action for money damages" and "complaint," those terms have their "ordinary or natural meaning." *FDIC* v. *Meyer*, 510 U.S. 471, 476 (1994) (construing undefined statutory term by reference to *Black's Law Dictionary*); accord *Pasquantino* v. *United States*, 544 U.S. 349, 356 (2005); *Dunn* v. *CFTC*, 519 U.S. 465, 470 (1997).

1. a. As then-Judge Roberts explained for the court of appeals, "[t]he phrase 'action for money damages' points strongly to a suit in a court of law, rather than an agency enforcement order that happens to concern money due under a statutory scheme." Pet. App. 16a. At the time of the statute's enactment, the term "action" was ordinarily understood to mean "[t]he legal and formal demand of one's right from another person or party made and insisted on *in a court of justice*. * * * Pursuit of right *in court*." *Black's Law Dictionary*, *supra*, at 49 (emphases added; citations omitted); see, *e.g.*, 1 Am. Jur. 2d *Actions* § 4, at 798 (2005) ("An 'action' is generally defined as a *judicial* proceeding in which one asserts a right or seeks redress for a wrong.") (emphasis added); 28 U.S.C. 2401(a) (using the terms "action" and "civil action" synonymously in a limitations provision); Fed. R. Civ. P. 2 ("There shall be one form of action to be known as 'civil action.'").[3]

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[3] One need look no farther than this Court's decisions from last June to confirm that the terms "action" and "administrative" are commonly juxtaposed in ordinary legal usage, with the former referring solely to court proceedings. See *Woodford* v. *Ngo*, 126 S. Ct. 2378, 2392 (2006) ("[A] prisoner may not bring an action with respect to prison conditions

The remainder of the statutory text buttresses the conclusion that an "action" is a suit in court. Congress referred not only to an "action," but to an "action for money damages." At the time of the statute's enactment, the term "damages" was ordinarily understood to mean "[a] pecuniary compensation or indemnity, which may be recovered in the courts." *Black's Law Dictionary*, *supra*, at 466. Especially when taken together, the phrase "action for money damages" has long been understood to refer to a particular type of suit in court. See, *e.g.*, *Chauffeurs Local No. 391* v. *Terry*, 494 U.S. 558, 570 (1990) ("Generally, an action for money damages was the traditional form of relief offered in the courts of law.") (internal quotation marks and citation omitted).

Significantly, the statute distinguishes between an "action" and an "administrative proceeding[]," with the time for filing an "action" beginning to run either upon accrual of the cause of action or upon completion of "applicable administrative proceedings required by contract or by law." 28 U.S.C. 2415(a). Administrative proceedings therefore trigger the limitations period; they are not "actions" governed by it. Section 2415(a)'s distinction between actions and administrative proceedings is not unusual—other statutes of limitations draw the same

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'until such administrative remedies as are available are exhausted.'") (quoting 42 U.S.C. 1997e(a)) (emphasis omitted); *Burlington N. & Santa Fe Ry.* v. *White*, 126 S. Ct. 2405, 2410 (2006) ("After exhausting administrative remedies, White filed this Title VII action."); *Arlington Cent. Sch. Dist. Bd. of Educ.* v. *Murphy*, 126 S. Ct. 2455, 2467-2468 (2006) (Breyer, J., dissenting) (referring disjunctively to "state administrative review or civil action," and again to "civil actions and administrative proceedings") (quoting H.R. Rep. No. 296, 99th Cong., 1st. Sess. 6 (1985) and H.R. Conf. Rep. No. 687, 99th Cong., 2d Sess. 7 (1986)) (emphasis omitted).

distinction by extending the time for filing an "action" in court until after the conclusion of administrative proceedings, reinforcing the distinction between administrative proceedings and actions in the statute-of-limitations context. See 15 U.S.C. 1691e(f)(1) (Equal Credit Opportunity Act); 46 U.S.C. App. 1292 (war risk insurance).

Other terms used in Section 2415, such as "right of action" and "defendant" (28 U.S.C. 2415(a) and (e)) also ordinarily refer to aspects of suits in court, not administrative proceedings. A "right of action" is ordinarily "[t]he right to bring *suit*; a legal right to maintain an action," with "suit" meaning "any proceeding * * * in a court of justice." *Black's Law Dictionary*, *supra*, at 1488 (emphasis added); cf. *Jackson Transit Auth.* v. *Local Div. 1285, Amalgamated Transit Union*, 457 U.S. 15, 21 (1982) (noting that "private right of action decisions address the * * * question whether Congress intended that a particular party be able to bring suit"). That a "right" of "action" is the right to bring a suit in court reinforces the conclusion that "action," as used in Section 2415(a), refers to a suit in court. The term "defendant" also ordinarily refers to a party to a suit in court. See *Black's Law Dictionary*, *supra*, at 507 (defining "defendant" to mean "[t]he person defending or denying; the party against whom relief or recovery is sought in an action or *suit*") (emphasis added).

b. As the court of appeals explained, any lingering doubt "is removed by the fact that subsection 2415(a) measures the limitations period from the filing of a 'complaint.'" Pet. App. 17a; accord *Phillips Petroleum Co.* v. *Johnson*, No. 93-1377, 1994 WL 484506, at *1 (5th Cir. Sept. 7, 1994) (36 F.3d 89 (Table)), cert. denied, 514 U.S. 1092 (1995). By requiring that the "complaint" be "filed

within" the specified period, Section 2415(a) contemplates that an action governed by the statute will commence with the filing of a complaint. 28 U.S.C. 2415(a). At the time of the statute's enactment, "complaint" was ordinarily understood to refer to "civil practice," where "[i]n those states having a Code of Civil Procedure, the complaint is the first or initiatory pleading on the part of the plaintiff in a civil action." *Black's Law Dictionary, supra*, at 356. That is the case with the Federal Rules of Civil Procedure, which provide that "[a] civil action is commenced by filing a complaint with the court." Fed. R. Civ. P. 3.

This Court therefore held in *Unexcelled Chemical Corp.* v. *United States*, 345 U.S. 59 (1953), that commencing an "action" by filing a "complaint" refers, in its "ordinary sense," to filing a complaint in court, not to initiating an administrative proceeding. *Id.* at 66. In *Unexcelled Chemical*, this Court construed a statute of limitations providing that "an action is commenced * * * on the date when the complaint is filed." *Ibid.* (quoting 29 U.S.C. 256). In holding that "the issuance of a formal complaint in the administrative proceedings" that preceded the lawsuit did not constitute commencement of the "action" for purposes of the statute of limitations, this Court explained that "[c]ommencement of an action by the filing of a complaint has too familiar a history" to be read as referring to the filing of an administrative pleading. *Ibid.*

That conclusion follows, *a fortiori*, for Section 2415, because the filing of the complaint is the relevant tolling event for both the general six-year statute of limitations and the one-year period "*after* final decisions have been rendered in applicable administrative proceedings required by contract or by law." 28 U.S.C. 2415(a) (em-

phasis added). Congress could not have meant to give the government one year from the end of administrative proceedings to commence administrative proceedings. Only in court could a complaint be filed *after* the conclusion of administrative proceedings. *Irwin Co.* v. *3525 Sage St. Assocs., Ltd.*, 37 F.3d 212, 214 n.1 (5th Cir. 1994). And because Section 2415 uses the term "complaint" for both the six-year and one-year periods, it clearly refers to the commencement of an action in court.

2. Petitioners argue (Pet. Br. 17-26) that the statutory terms "action" and "complaint" are sometimes used to refer to administrative proceedings. But those are far from the ordinary meanings of those terms, as just explained, and the canon requiring strict construction of limitations periods against the government counsels against giving those terms a broader reading here. Moreover, the statutory phrase must be read as a whole, and "[t]aken together, the entire [statutory] phrase plainly and indisputably refers to lawsuits brought by the federal government." Pet. App. 17a (quoting *OXY USA, Inc.* v. *Babbitt*, 268 F.3d 1001, 1010 (10th Cir. 2001) (en banc) (Briscoe, J., dissenting)). The authorities relied on by petitioners are not to the contrary.

a. Petitioners first argue (Pet. Br. 17-18) that this Court "construed the term 'action' to encompass administrative actions" in *West* v. *Gibson*, 527 U.S. 212 (1999), and *Pennsylvania* v. *Delaware Valley Citizens' Council for Clean Air*, 478 U.S. 546 (1986). Not so. In *West*, the majority and dissenters alike agreed that "the word 'action' often refers to judicial cases, not to administrative 'proceedings.'" 527 U.S. at 220 (citing *New York Gaslight Club, Inc.* v. *Carey*, 447 U.S. 54, 60-62 (1980), as "distinguishing civil 'actions' from administrative 'pro-

ceedings'"); accord *id.* at 227 (Kennedy, J., dissenting) ("[T]he word 'action' is often used to distinguish judicial cases from administrative 'proceedings.'").

The *West* Court held that the Equal Employment Opportunity Commission's authority to award "appropriate remedies" in Title VII cases against government agencies under 42 U.S.C. 2000e-16(b) includes authority to award compensatory damages. 527 U.S. at 217. In doing so, the Court rejected the contention that because a separate statutory provision authorizes recovery of compensatory damages "[i]n an action" (42 U.S.C. 1981a(a)(1)), such damages are available only in court. Notwithstanding petitioners' contrary characterization (Pet. Br. 18), the Court explained that the question was *not* whether the term "action" includes administrative proceedings, but whether Congress's authorization of compensatory damages in an "action" was "intended to deny that compensatory damages is '*appropriate*' administrative relief" under the *separate* provision governing administrative remedies. *West*, 527 U.S. at 220-221. By resting its decision on the authorization for appropriate administrative relief, this Court appeared to recognize that the separate provision governing compensatory damages in an "action" applied only to suits in court.

Petitioners' reliance (Pet. Br. 17-18) on *Delaware Valley Citizens' Council* fares no better. There this Court construed 42 U.S.C. 7604(d), which provides that a court may award "costs of litigation" in "any action" brought under a provision of the Clean Air Act, 42 U.S.C. 7401 *et seq.* This Court held that *when a plaintiff prevails in a suit in court*, its recovery of the costs of litigation can include out-of-court costs of monitoring the defendant's compliance with a consent decree and

attempting to ensure compliance, including in administrative fora. 478 U.S. at 558-559. In such circumstances, a court issues the award in a court "action," not an administrative proceeding, and this Court explained that the compensable out-of-court work was "as necessary to the attainment of adequate relief" as "th[e] earlier work in the courtroom." *Id.* at 558. The Court also saw no reason to believe that Congress intended a different result under Section 7604(d) than would obtain under another statute that authorizes the recovery of litigation costs in "'any action or proceeding' brought to enforce the Civil Rights Acts." *Id.* at 559 (quoting 42 U.S.C. 1988(b)).

Significantly, the Court in *Delaware Valley Citizens' Council* "express[ed] no judgment on the question whether an award of attorney's fees is appropriate in federal administrative proceedings when there is no connected court action in which fees are recoverable." 478 U.S. at 560 n.5. Nor did the Court address a statute of limitations concerning the federal government's filing of a complaint in an action for money damages. Thus, *Delaware Valley Citizens' Council* sheds no light on the interpretive question here.

b. Petitioners argue (Pet. Br. 18-21) that various statutes and regulations illustrate that the word "action" can include administrative proceedings. Unlike Section 2415(a), however, every single authority cited by petitioners expressly states that it applies to administrative as well as judicial proceedings, such as by using the term "administrative action," *e.g.*, 42 U.S.C. 5205(a)(1), or by using an inclusive phrase like "an administrative, civil, or criminal action," *e.g.*, 15 U.S.C. 78u(h)(9)(B). Far from supporting petitioners' contention that the term "action" standing alone includes administrative

proceedings, those provisions suggest that when Congress intends a phrase that includes the word "action" to govern administrative proceedings, it says so expressly.[4]

c. Similarly, petitioners rely (Pet. Br. 22-23) on the fact that some administrative proceedings begin with the filing of a document called a "complaint." As explained above, however, the ordinary meaning of the term "complaint" does not include administrative filings, especially in statutes of limitations governing the commencement of actions, and especially here, where the time for filing a complaint is based in part on the termination of administrative proceedings. See *Unexcelled Chem. Corp.*, 345 U.S. at 66; pp. 17-18, *supra*.

It would, moreover, make little sense to base a general limitations period for administrative proceedings on the filing of a "complaint." While judicial proceedings invariably begin with the filing of a "complaint" or functionally similar document, administrative procedures vary substantially, requiring limitations periods for such proceedings to use different terminology tailored to specific contexts. For example, 15 U.S.C. 4504(a)(2), which governs some enforcement actions by the Secretary of Energy, applies its limitations period for a lawsuit to "the filing of a complaint," but applies its limitations period for administrative proceedings to "the signing

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[4] Although petitioners emphasize (Pet. Br. 21) that MMS has occasionally referred in passing to its administrative proceedings as "actions," MMS has not construed its proceedings to be "actions" within the meaning of Section 2415. The question here is not whether the term "action" is sometimes used broadly or loosely to refer to administrative proceedings, but whether its ordinary meaning, in the context of Section 2415(a)'s limitations provision and the other relevant terms in that section like "complaint" and "right of action," encompasses such proceedings.

and issuance of a proposed remedial order." The Contract Disputes Act of 1978, 41 U.S.C. 601 *et seq.*, which governs many government contract claims, see 41 U.S.C. 602, requires that "each *claim* by the government against a contractor relating to a contract shall be *submitted*" to a contracting officer within six years of the claim's accrual, 41 U.S.C. 605(a) (emphases added). Other administrative limitations periods likewise refer to events other than the filing of a complaint. See, *e.g.*, 31 U.S.C. 3808 (limitations period for "commenc[ing]" a "hearing"); 42 U.S.C. 9612(d) (limitations period for "present[ing]" a "claim"); 42 U.S.C. 1320a-7a(c)(1) (limitations period for "initiat[ing] a proceeding").

As the court of appeals recognized, this case provides a prime example of an administrative scheme that does not involve the filing of a "complaint." Pet. App. 17a. If an audit reveals an apparent underpayment by a lessee, MMS typically sends the lessee an issue letter and requests a response. See *Phillips Petroleum Co.* v. *Lujan*, 963 F.2d 1380, 1386 (10th Cir. 1992); *In re Amoco Prod. Co.*, 123 I.B.L.A. 278, 292 (1992) (Hughes, J., concurring). After reviewing the response, MMS will issue, if appropriate, an order to pay that is legally binding unless the lessee takes an administrative appeal and obtains a suspension of the order pending appeal by posting a bond or demonstrating financial solvency. See 30 C.F.R. 218.50(c), 243.8. There is no "complaint" in that scheme; instead, there is (i) informal process, followed by (ii) an order imposing (not requesting) relief, and (iii) an administrative appeal. When Congress enacted a prospective seven-year limitations period actually addressed to federal oil and gas royalties, it therefore applied that period not to the filing of a complaint, but to the commencement of a "judicial proceeding or de-

mand," 30 U.S.C. 1724(b)(1), and it defined the term "demand" to include "an order to pay issued by the Secretary," 30 U.S.C. 1702(23).

Although petitioners argue (Pet. Br. 23 & n.11) that MMS's orders should be treated as complaints for this purpose, the court of appeals correctly explained that "[i]t strains legal language to construe [MMS's] administrative compliance order as a 'complaint' for money damages in any ordinary sense of the term." Pet. App. 17a; accord *Phillips Petroleum*, 1994 WL 484506, at *1. A complaint seeks relief; an order imposes it. Compare *Black's Law Dictionary*, *supra*, at 356 (defining "complaint" to mean the "first or initiatory pleading on the part of the plaintiff in a civil action") with *id.* at 1247 (defining "order" to mean a "mandate, precept; a command or direction authoritatively given; a rule or regulation"). See 5 U.S.C. 551(6) (defining "order" for purposes of the Administrative Procedure Act as "the whole or a part of a final disposition, whether affirmative, negative, injunctive, or declaratory in form, of an agency in a matter other than rulemaking but including licensing").

Petitioners' response (Pet. Br. 23-24 n.11)—that "[a]n agency cannot evade the six-year limitations period simply by calling the document that commences proceedings something other than a 'complaint'"—ignores the fact that MMS's orders do not "initiate proceedings for the recovery of royalties," as petitioners claim. *Id.* at 24 n.11. Instead, as explained above, MMS's orders *command* the payment of royalties following an audit and informal agency process, and an order is legally binding unless a lessee brings a successful appeal and MMS suspends the order pending appeal. See Pet. App. 17a; p. 22, *supra*.

There are two lessons to be drawn from Section 2415(a)'s use of the term "complaint." First, Congress did not have administrative proceedings in mind. And second, even if some administrative pleadings were governed by the limitations period, MMS's orders would not be.[5]

### B. The Statutory Context Confirms That The Limitations Period Does Not Apply to Administrative Proceedings

The statutory context confirms that Section 2415 does not govern administrative proceedings. Section 2415 is located within Title 28 of the United States Code, which is entitled "Judiciary and Judicial Procedure"—not "Administrative Procedure," which is governed by Chapter 5 of Title 5. Moreover, Section 2415 is included in Title 28's Chapter 161, which governs the Judiciary and judicial procedure specifically in cases involving the "United States As Party Generally."

The other provisions of Chapter 161 apply only to cases in court, not to administrative proceedings. And like Section 2415(a), several of them use the term "action" to describe their scope as being limited to suits in court. See, *e.g.*, 28 U.S.C. 2402 (delineating the jury trial right in "any action" against the United States); 28 U.S.C. 2403 (governing intervention by the United States in an "action, suit or proceeding in a court of the United States"); 28 U.S.C. 2405 (debtors summoned as possible garnishees in an "action or suit commenced by

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[5] Petitioners argue (Pet. Br. 15, 26) that Section 2415(a) should be construed broadly because it applies to "every" action for money damages founded upon a contract and initiated by a complaint. Of course, a statute that covers *every* action in court still does not cover *any* administrative proceedings.

the United States" shall "appear in open court"); 28 U.S.C. 2406 ("[i]n an action by the United States," a defendant's ability to assert a credit depends in part on its possession of vouchers "at the time of trial"); 28 U.S.C. 2407 (governing procedure by a "court" in "an action by the United States" against a person accountable for public money).[6]

Section 2415's location in Chapter 161 of the Judicial Code is no accident—Congress specified that placement when it enacted the limitations period. Act of July 18, 1966, Pub. L. No. 89-505, 80 Stat. 304; see H.R. Rep. No. 1534, 89th Cong., 2d Sess. 2 (1966) (explaining that Section 2415 would be added to Chapter 161, "a chapter which contains the general provisions applying to the United States as a party in litigation"). Congress's placement of Section 2415 in Chapter 161 further demonstrates that it intended the provision to govern only suits in court, not administrative proceedings. Cf. *Almendarez-Torres* v. *United States*, 523 U.S. 224, 234 (1998) ("'[T]he title of a statute and the heading of a section' are 'tools available for the resolution of a doubt' about the meaning of a statute.") (quoting *Brotherhood*

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[6] See also 28 U.S.C. 2401 (general statute of limitations for commencing a "civil action" against the United States); 28 U.S.C. 2404 (effect of defendant's death in "a civil action for damages" brought by the United States); 28 U.S.C. 2408 (security for damages or costs not required of the United States); 28 U.S.C. 2409 (procedure in civil action for partition of lands); 28 U.S.C. 2409a (procedure in civil action to quiet title to real property); 28 U.S.C. 2410 (procedure in civil action "in any district court" involving property on which the United States has a lien); 28 U.S.C. 2411 (interest to be included in a judgment of a "court"); 28 U.S.C. 2412 (award of costs and fees by a "court"); 28 U.S.C. 2413 (execution of judgment rendered by a "court"); 28 U.S.C. 2414 (payment of judgments rendered by a "court").

*of R.R. Trainmen* v. *Baltimore & Ohio R.R.*, 331 U.S. 519, 528-529 (1947)).

Moreover, Congress has shown that when it intends a limitations period to apply to administrative proceedings, it knows how to say so.[7] When Congress has wanted the same limitations period to apply to both administrative and judicial proceedings, it has said that expressly, too, including in the prospective limitations period governing a "judicial proceeding or demand" for federal oil and gas royalties. 30 U.S.C. 1724(b)(1).[8] Thus, petitioners' contention (Pet. Br. 25-26) that the statute should be construed broadly to cover administrative proceedings because it is not expressly limited to suits in court ignores not only the ordinary meanings of the statutory terms, the statutory context, and the narrow construction canon, but also the fact that Congress has generally followed the opposite course by affirmatively specifying when a limitations period applies to administrative proceedings.

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[7] See, *e.g.*, 42 U.S.C. 1320a-7a(c)(1) (limitations period for administrative "proceeding"); 42 U.S.C. 5205(a)(1) (limitations period for "administrative action[s]"); 42 U.S.C. 9612(d) (limitations periods for administrative claims procedure).

[8] See, *e.g.*, 15 U.S.C. 4504(a)(1) and (3) (defining a "civil enforcement action" to include an "administrative or judicial civil action" in a statute of limitations provision); 21 U.S.C. 335b(b)(1) and (3) (classifying an administrative remedy as an "[a]ction by the Secretary" and a judicial remedy as an "[a]ction by the Attorney General" in specifying the statute of limitations for every "action"); 38 U.S.C. 5314(c) (specifying that there is no limitations period either for "bringing civil actions or for commencing administrative proceedings"); 12 U.S.C. 1787(6)(B) (providing the same period to "request administrative review" or "file suit"); 12 U.S.C. 1821(d)(6)(B) (same); cf. 31 U.S.C. 3712(d) ("The Government waives all claims * * * not reported to the Comptroller General for collection within 6 years.").

### C. The Legislative History Confirms the Import of the Plain Text

The legislative history of Section 2415(a) confirms that it means what it says.

1. The committee reports explain that Section 2415(a) "defines the time limitations for the United States to bring *actions in the U.S. courts*" by barring the government from asserting "old and stale claims *in the courts*." H.R. Rep. No. 1534, *supra*, at 2, 9 (emphases added); see S. Rep No. 1328, 89th Cong., 2d Sess. 1-10 (1966) (quoting the House report as the Senate report). The reports go on to confirm that Section 2415(a) applies to a "civil action," and they are replete with references to the United States bringing "suit." *E.g.*, H.R. Rep. No. 1534, *supra*, at 2, 4, 8, 9, 10, 11. As petitioners concede (Pet. Br. 24), those terms refer to judicial proceedings. See, *e.g.*, *Black's Law Dictionary*, *supra*, at 1603 (defining "suit" to mean "any proceeding * * * in a court of justice"); *id.* at 311 (defining "civil action" to mean "[a]n action wherein an issue is presented for trial"). With additional references to "civil litigation" and "court congestion," the reports are replete with court terminology. *E.g.*, H.R. Rep. No. 1534, *supra*, at 3.

In contrast, the reports limit their discussion of administrative proceedings to explaining that the limitations period expires no sooner than "a year after the final administrative decision." H.R. Rep. No. 1534, *supra*, at 4; see S. Rep. No. 1328, *supra*, at 3. Of course, that only underscores the statutory text's distinction between "actions" and "administrative proceedings." Moreover, the reports explain that it was necessary to extend the limitations period until after the conclusion

of administrative proceedings "because of the great number and variety of such proceedings." H.R. Rep. No. 1534, *supra*, at 4; see S. Rep. No. 1328, *supra*, at 3. That further confirms that Congress did not intend to enact a one-size-fits-all limitations period for the commencement of the variety of administrative proceedings, but instead intended that Section 2415(a)'s limitations period would not expire until after administrative proceedings produced a final decision, a term with both familiar meaning in administrative law and uniform content across the range of administrative proceedings.

The proposed legislation was forwarded to Congress by the Department of Justice, which represents the United States in courts (see 28 U.S.C. 516), not by any other agency with authority for a particular administrative program. See H.R. Rep. No. 1534, *supra*, at 9-14. The Attorney General's letter to Congress explains that Section 2415, in conjunction with companion legislation concerning actions against the government, would "improve the disposition of monetary claims by and against the Government—claims which now comprise the bulk of *civil litigation* involving the Government." *Id.* at 9 (emphasis added). The Attorney General's recommendation also discusses "suits" as the subject of the legislation, *id.* at 11, and explains that the limitations period would "ease court congestion," resulting in "removal from the courts of litigation." *Id.* at 9, 12. In contrast to those repeated references to suits in court, the Attorney General's recommendation makes no mention of administrative proceedings.

The legislative hearings contain numerous similar references to "court claims," "suits," "civil litigation," and "reduc[ing] unnecessary litigation and court congestion." *Improvement of Procedures in Claims Settlement*

*and Government Litigation: Hearing Before Subcomm. No. 2 of the House Comm. on the Judiciary*, 89th Cong., 2d Sess. 5, 6, 7, 9, 10 (1966) (statement of John W. Douglas, Asst. Att'y Gen., Civil Div., Dep't of Justice, on H.R. 13652). In sum, the contemporaneous legislative history leaves little doubt that Congress addressed litigation in the courts, not the variety of agency proceedings that could involve the collection of money.

2. Petitioners mostly avoid Section 2415(a)'s legislative history. While they assert (Pet. Br. 40) that "it was the potential abuse of *administrative* processes that led to Section 2415's enactment," they cite nothing in the legislative history of Section 2415 that supports that statement. Instead, petitioners rely on a brief observation made by one Member of the House of Representatives during a hearing before the House Government Operations Committee that addressed a variety of issues concerning Defense Department and General Accounting Office auditing procedures. See *id.* at 41-42. There is no reason to believe that the brief remark relied on by petitioners influenced the later proposal of Section 2415 by the Justice Department, consideration of the bill by a different committee in the House (the Judiciary Committee), and the statute's enactment by the full Congress.

To the contrary, the House Report on the bill that enacted Section 2415 correctly notes that the report of the Government Operations Committee had expressed a need for "a statute of limitations which would apply to *suits* by the government." H.R. Rep. No. 1534, *supra*, at 8 (emphasis added); see H.R. Rep. No. 1344, 89th Cong., 2d Sess. 16 (1966) (recommending the development of "recommendations with respect to application of the statute of limitations to *suits* by the government")

(emphasis added). Petitioners point to nothing in the history of the legislation that enacted Section 2415 (including subsection (a) at issue here) suggesting that Congress intended to reach beyond suits in court to regulate the issuance of administrative orders.

3. Equally misplaced is petitioners' reliance (Pet. Br. 26-30, 44-45) on subsequent legislation. Of course, "[t]he views of a subsequent Congress form a hazardous basis for inferring the intent of an earlier one." *Mackey* v. *Lanier Collection Agency & Serv., Inc.*, 486 U.S. 825, 840 (1988) (quoting *United States* v. *Price*, 361 U.S. 304, 313 (1960)). In any event, neither the subsequent legislation nor its legislative history suggests that any Congress ever thought that Section 2415 applied to administrative proceedings or attempted to extend it to those proceedings.

a. Petitioners rely primarily (Pet. Br. 26-30) on 28 U.S.C. 2415(i), which provides that "[t]he provisions of [28 U.S.C. 2415(a)] shall not prevent the United States or an officer or agency thereof from collecting any claim of the United States by means of administrative offset, in accordance with section 3716 of title 31." That provision, which was enacted 16 years after Section 2415(a), resolved a specific dispute about administrative offsets by clarifying that the statute does not apply to them; it did not expand the statute's coverage to other administrative proceedings.

As the court of appeals explained (Pet. App. 18a-19a), and petitioners concede (Pet. Br. 28-30 & n.17), the Comptroller General disagreed with the Department of Justice's Office of Legal Counsel (OLC) about whether Section 2415(a) applied to administrative offsets, and recommended the enactment of Section 2415(i) "as a means of resolving the differences between us." *Debt*

*Collection Act of 1981: Hearings on S. 1249 Before the Senate Comm. on Governmental Affairs*, 97th Cong., 1st Sess. 83 (1981) (statement of Milton J. Socolar, Acting Comptroller Gen.). The Senate Report explains that Congress intended the amendment to "clarify[]" that the limitations period does not apply to administrative offsets. S. Rep. No. 378, 97th Cong., 2d Sess. 2 (1982); see *id.* at 16 (describing the amendment's "[c]larification" on that point). Petitioners can point to nothing suggesting that Congress intended to do anything other than address the specific dispute before it. If anything, Congress's "clarif[ication]" that Section 2415(a) does not govern administrative offsets suggests that Congress thought the statute did not apply to administrative proceedings generally. *Id.* at 2.

Although petitioners argue (Pet. Br. 26-27) that Section 2415(i) should not be read to be surplusage, administrative offsets are different from other administrative proceedings. In opining that offsets were subject to Section 2415(a)'s limitations period, OLC explained that "[w]here the debt has not been reduced to judgment, an administrative offset is merely a pre-judgment attachment device. Thus, if no possibility of obtaining a judgment on the alleged debt exists, the administrative offset cannot be used." Memorandum from John M. Harmon, Asst. Att'y Gen., OLC, Dep't of Justice, to Alan K. Campbell, Chairman, U.S. Civil Serv. Comm'n, *Effect of Statute of Limitations on Admin. Collection of U.S. Claims* 3-4 (Sept. 29, 1978); see *id.* at 9 n.3 ("this administrative procedure is merely a pre-judgment attachment device"). An administrative adjudication presents a different question because it functions as a judgment of liability, not merely as a pre-judgment attachment.

Moreover, giving effect to Section 2415(a)'s plain terms as applying its limitations periods only to court actions does not render Section 2415(i) superfluous. The question OLC addressed arose in a situation where the debt the government sought to collect was to be offset against the government's ongoing payment of benefits under another provision—in that case, the Civil Service Retirement Program—even in the absence of a discrete claim against the United States. If the debt the government sought to collect could otherwise be enforced only through an affirmative action in court, and an action in court on that debt would be barred by Section 2415(a), Section 2415(i) clarifies that such an offset is not time-barred. The question whether an otherwise time-barred claim can be used defensively as an offset in that manner arises whether or not Section 2415(a) limits only court actions or both court actions and administrative proceedings brought by the government. The addition of Section 2415(i) therefore does not suggest that Section 2415(a) applies to the institution of administrative proceedings.

In any event, as the court of appeals explained, the "preference for avoiding surplusage constructions is not absolute." Pet. App. 18a (quoting *Lamie* v. *U.S. Trustee*, 540 U.S. 526, 536 (2004)); accord *Chickasaw Nation* v. *United States*, 534 U.S. 84, 94 (2001). Because Congress acted to clarify a specific, disputed question of law, the 1982 amendment should not be read more broadly. *O'Gilvie* v. *United States*, 519 U.S. 79, 89-90 (1996); see *United States* v. *Vonn*, 535 U.S. 55, 71 (2002) ("Having pinpointed th[e] problem, [Congress] gave a pinpoint answer."). Moreover, plain statutory text trumps the surplusage canon. See, *e.g.*, *Lamie*, 540 U.S. at 536. That point applies with special force here because the

text must be construed strictly in favor of the government, and the statutory context and legislative history confirm the text's ordinary meaning. As the court of appeals emphasized, "[e]xpanding the apparent scope of a statute of limitations beyond its plain language by inference from an express exception is hardly strict construction." Pet. App. 19a.

Finally, if Section 2415 did not reach administrative proceedings before the addition of subsection (i), it cannot seriously be maintained that Congress would have taken the significant step of extending the limitations period to all manner of administrative proceedings through the elliptical route of exempting administrative offsets. Congress would have had many more direct routes to accomplish that significant step, which only reinforces subsection (i)'s status as a minor clarification, not a major extension, of Section 2415's reach.[9]

b. Although petitioners also rely (Pet. Br. 44-45) on amendments to Section 2415 that extended the limitations periods for some Indian claims, those amendments and their legislative history only confirm that the limitations period does not apply to administrative proceedings. In 1972, Congress amended Section 2415(a) to extend the time for filing "an action for money damages" on behalf of Indian Tribes, bands, and groups. Act of Oct. 13, 1972, Pub. L. No. 92-485, 86 Stat. 803. Like the committee reports concerning the original Section

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[9] Petitioners suggest there is something anomalous about subjecting affirmative administrative actions to no time limit, while offsets are limited to a ten-year period. But affirmative administrative actions may be limited by context-specific limitations periods. See, *e.g.*, 30 U.S.C. 1724(b)(1). Likewise, because administrative offsets might be available for claims that could otherwise only be enforced in courts, an outer limit on offsets complements the limitations on court actions.

2415(a), the committee reports on the amendment are full of references to "suits" and "litigation," but not to administrative proceedings. *E.g.*, H.R. Rep. No. 1267, 92d Cong., 2d Sess. 3 (1972); S. Rep. No. 1253, 92d Cong., 2d Sess. 2 (1972). Indeed, they state that "the cost to the United States government" of pursuing the affected claims "would be limited to the costs of prosecuting the claims *in the courts*." H.R. Rep. No. 1267, *supra*, at 4 (emphasis added); S. Rep. No. 1253, *supra*, at 3 (emphasis added). In the hearing transcript cited by petitioners (Pet. Br. 44-45), the very witness whose testimony is relied upon by petitioners likewise explained that "[t]hese are claims that would be filed in the Federal district court." *Time Extension for Commencing Actions on Behalf of Indians: Hearing Before the Subcomm. on Indian Affairs of the Senate Comm. on Interior and Insular Affairs*, 92d Cong., 2d Sess. 31 (1972) (Arthur Lazarus, Jr.). While petitioners are correct (Pet. Br. 45) that extensions of the limitations period would have been unnecessary if Congress had been concerned only with administrative collection of oil and gas royalties under the MLA, Congress enacted those extensions to protect the broader range of Indian claims brought in the courts.[10]

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[10] Congress later required the Department of the Interior to publish a list of some Indian claims, and it extended the limitations period for each of those claims until after the date the claim is listed, the date the Secretary submits a legislative proposal to resolve the claim, or the date the Secretary rejects the claim "for litigation." Indian Claims Limitation Act of 1982, Pub. L. No. 97-394, §§ 3-6, 96 Stat. 1976-1978. That reference to "litigation" in this context further suggests that Congress was concerned with suits in courts, not administrative orders. The Secretary explained in publishing the required list that "[t]he vast majority of the listed claims involve trespasses to Indian land," 48 Fed. Reg. 51,204 (1983)—claims that would necessarily be heard in court.

### D. Petitioners' Reliance On One Of The General Purposes Of Section 2415 Is Misplaced

Petitioners argue at length (Pet. Br. 31-40) that Section 2415(a) should be read broadly to promote general policies of fairness and repose. As the court of appeals explained, "such appeals to purpose cannot override a statute's clear language," Pet. App. 20a, especially where, as here, the statute must be strictly construed in favor of the government. *Badaracco*, 464 U.S. at 398. And because "no legislation pursues its purposes at all costs," "it frustrates rather than effectuates legislative intent simplistically to assume that *whatever* furthers the statute's primary objective must be the law." *Rodriguez* v. *United States*, 480 U.S. 522, 525-526 (1987) (per curiam); see *ibid.* ("Deciding what competing values will or will not be sacrificed to the achievement of a particular objective is the very essence of legislative choice."). In any event, the statutory policies do not support petitioners' attempt to extend Section 2415 to administrative proceedings, especially the MMS orders at issue here.

1. Petitioners err in arguing (Pet. Br. 33-34) that application of the limitations period to administrative proceedings is necessary to fulfill a congressional purpose "to place the government on (mostly) equal footing with private parties." The legislative history expresses an intent only "to provide a more balanced * * * treatment of *litigants in civil actions* involving the government." H.R. Rep. No. 1534, *supra*, at 3 (emphasis added). While "(mostly) equal footing" might be a meaningful concept in court cases, it has little application to administrative proceedings that only the agency can

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See generally *County of Oneida* v. *Oneida Indian Nation*, 470 U.S. 226, 241-244 (1985) (discussing background of 1982 amendments).

initiate, and in which the agency is charged with interpreting the governing statutes and regulations and is often fulfilling a trust responsibility to affected Indians. In that context, the agency acts as a regulator, not as a private party filing a commercial contract suit in court.

2. That conclusion is reinforced by the special circumstances of the government's mineral leasing program and by Congress's response.

a. Congress enacted FOGRMA in 1982 because oil and gas lessees were underpaying royalties by staggering amounts—up to half a billion dollars annually. H.R. Rep. No. 859, 97th Cong., 2d Sess. 16 (1982); see *id.* at 46 (discussing the "many instances of gross underpayment and nonpayment of royalties"). Congress responded by directing MMS to "audit and reconcile, to the extent practicable, *all current and past* lease accounts for leases of oil or gas and [to] take appropriate actions to make additional collections or refunds as warranted." 30 U.S.C. 1711(c)(1) (emphasis added). The House Report stressed that "the Committee expects the Department to continue to place high priority on reconciling *old* accounts." H.R. Rep. No. 859, *supra*, at 33 (emphasis added). Congress's emphatic direction to the Secretary to conduct such an audit of past lease accounts because of a history of massive underpayment hardly manifests an intent to limit liability for past misconduct.

Because lessees calculate their own royalty obligations, underpayments are especially difficult to identify in this context. MMS cannot realistically audit every royalty account. Recognizing that constraint, Congress instead required audits "to the extent practicable," and directed the Secretary to give priority to auditing some leases while selectively auditing others. 30 U.S.C. 1711.

Such audits can detect systematic underpayment dating back more than six years. The absence of a limitations period for administrative orders in this setting is entirely understandable—especially because many of the affected leases are on lands owned by Indians or Indian Tribes to whom the United States owes trust responsibilities. See, *e.g.*, 30 U.S.C. 1701(a)(4) and (b)(4).[11]

b. Petitioners miss the mark in arguing (Pet. Br. 36-37) that the applicability of a limitations period should not turn on MMS's choice to proceed administratively instead of in court. FOGRMA contemplates effective administrative enforcement. It requires the Secretary to establish a comprehensive auditing and *collection* system, 30 U.S.C. 1711(a), and it empowers the Secretary to enforce his orders administratively by imposing penalties of up to $10,000 for each day a lessee fails to comply with an order, 30 U.S.C. 1719(c)(1). Although the Attorney General may bring a civil action for equitable relief to require compliance with any federal mineral leasing law, 30 U.S.C. 1722(a), the Department of the Interior is not aware of any instance in which recourse to the courts was necessary to require compliance with

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[11] There is no reason to attribute the absence of such a limitations period to oversight. The MLA and FOGRMA contain two limitations periods: one for the commencement of an "action contesting a decision of the Secretary," 30 U.S.C. 226-2, and another for the recovery of penalties, 30 U.S.C. 1755. Congress thereby demonstrated an awareness of limitations issues, and chose to enact limitations periods for matters *other than* the issuance of orders directing a lessee to pay past-due royalties or otherwise to comply with statutory and regulatory requirements.

an order to pay. Instead, MMS administratively imposes civil penalties to enforce its orders.[12]

c. As the mineral-leasing context illustrates, there is little reason to assume that Congress would want the same general limitations period that governs suits in court to apply to administrative proceedings. There are substantial procedural and other differences between court suits and administrative proceedings, and administrative proceedings themselves differ from context to context. One salient difference is that, in our liberal notice pleading system, a court complaint is expected to

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[12] If an especially determined lessee were unwilling to comply with an order to pay and remained undeterred by administrative penalties, the Attorney General would have at least one year from the final administrative decision to file suit to enforce the royalty order. Assuming, *arguendo*, that an action to enforce an order to pay would seek "money damages" "founded upon * * * [a] contract," and thus be governed by Section 2415(a), the limitations period would run no earlier than "one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law." 28 U.S.C. 2415(a). Petitioners err in asserting (Pet. Br. 43 n.23) that MMS's administrative proceedings are not required by law. FOGRMA requires MMS not only to conduct audits, but also to establish a comprehensive system for collecting royalties. 30 U.S.C. 1711(a). When an audit reveals an underpayment, MMS discharges that responsibility by sending an issue letter and, if appropriate, issuing an order to pay. See p. 22, *supra*. The ensuing administrative appeals are required by law as a precondition to seeking judicial review. See 30 C.F.R. 290.110 (outlining the requirements for exhausting administrative remedies). A contrary conclusion would be perverse, because Congress obviously intended the one-year period to permit agencies to conclude administrative proceedings before filing in court. See H.R. Rep. No. 1534, *supra*, at 4 (explaining that the one-year period is necessary "because of the great number and variety of [administrative] proceedings"); cf. *Mesa Operating Ltd. P'ship* v. *Department of the Interior*, 17 F.3d 1288, 1291-1292 (10th Cir. 1994) (explaining how Section 2415(a) would apply to a judicial enforcement action by MMS).

be short and concise, and allegations can be made on information and belief. See Fed. R. Civ. P. 8, 11. In contrast, for example, MMS must undertake far more effort before issuing an order. MMS or a State with delegated authority must conduct an audit to determine whether a lessee has made correct royalty payments. Then MMS typically provides informal administrative process by sending an issue letter to the lessee and awaiting a response before deciding whether to issue an order to pay. See p. 22, *supra*.

Congress thus had good reason not to subject MMS's administrative orders to the same general limitations period that governs complaints filed in court. Doing so would penalize MMS for affording informal process before issuing an order, because the limitations period would ordinarily continue to run while MMS awaited the lessee's response and decided whether to issue an order. Congress evidently recognized that difficulty, because when it enacted a prospective limitations period in 1996 for MMS's orders to pay royalties for oil and gas production on federal lands, it selected a period of seven—not six—years. 30 U.S.C. 1724(b)(1).

3. Petitioners greatly overstate the potential harms they face from having to make good on royalties they systematically withheld for more than six years. Petitioners argue (Pet. Br. 37-38) that records from earlier time periods may have been destroyed, as permitted by FOGRMA. There are two problems with that argument. First, although records ordinarily need only be kept for six years, "such records must be maintained for a longer period" if "the Secretary notifies the record holder that he has initiated an audit or investigation involving such records." 30 U.S.C. 1713(b). Petitioners therefore err in arguing (Pet. Br. 32-33, 38) that FOGRMA's record-

retention provisions suggest that a six-year statute of limitations applies.[13] Second, the lawful destruction of records would make the issuance of an order to pay unlikely. Without records to audit and review, it would often be impractical for MMS to conduct an audit and determine the amount of any underpayment.

Although petitioners also emphasize (Pet. Br. 38-39) that lessees must pay interest on past-due royalties, interest payments merely compensate for the time value of money, *i.e.*, the fact that the lessee benefitted from retaining and using money that it should have paid to the government or an Indian lessor. As this Court has explained, "prejudgment interest is not awarded as a penalty; it is merely an element of just compensation." *City of Milwaukee* v. *Cement Div., Nat'l Gypsum Co.*, 515 U.S. 189, 197 (1995); see Pet. Br. 50.

Petitioners profess concern (Pet. Br. 36) that MMS could seek royalties dating back "in perpetuity," but they cite no instance in which MMS has done anything like that. Here, only about 20 months are in dispute, because MMS's May 1997 order extends back to January 1989—approximately 29 months longer than petitioners consider appropriate, with nine of those months covered by a tolling agreement the parties entered into during the administrative proceedings. See Amoco Admin. R. 842, 844, 846.

4. The bottom line is that Congress may choose to address a problem in stages, and it is not the province of the courts to rewrite a statute in hopes of better achiev-

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[13] In some instances, the Secretary might be able to recover royalties for the older periods even if Section 2415(a) applied, because the limitations period does not run when "facts material to the right of action are not known and reasonably could not be known" by a responsible government official. 28 U.S.C. 2416(c).

ing one of Congress's purposes. *Director, Office of Workers' Compensation Programs, Dep't of Labor* v. *Newport News Shipbuilding & Dry Dock Co.*, 514 U.S. 122, 135-136 (1995). The question whether Section 2415(a) applies to administrative proceedings has arisen primarily in the context of mineral leases under the MLA. When Congress became aware of that issue, it enacted a limitations period in 1996 for oil and gas leases on federal lands, but it applied that new limitations period only prospectively, it chose a *longer* period than would apply under Section 2415(a), and it did not apply that new limitations period to federal leases of minerals other than oil and gas or to any Indian leases. 30 U.S.C. 1724(b). Reading Section 2415(a) to apply to administrative proceedings would produce the bizarre result that a shorter limitations period would apply to Indian leases than to federal leases, notwithstanding Congress's express purpose to "fulfill the trust responsibility of the United States for the administration of Indian oil and gas resources." 30 U.S.C. 1701(b)(4); see 30 U.S.C. 1701(a)(4) ("the Secretary should aggressively carry out his trust responsibility"). For those reasons, and given the clear text, context, and legislative history of Section 2415(a), further adjustment of the limitations periods is a fundamentally legislative task.[14]

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[14] Because the court of appeals held that MMS's order was not a "complaint" in an "action," it did not reach respondents' alternative arguments that the order did not seek money damages and was not founded upon a contract within the meaning of Section 2415(a). Pet. App. 20a; see Gov't Pet.-stage Br. 17-19. Petitioners are correct (Pet. Br. 45) that there is no reason for this Court to depart from its normal practice of considering only the issues decided below. If this Court were to disagree with the court of appeals' decision, respondents could renew their alternative arguments on remand.

## CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

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AUGUST 2006

1367

No. 05-669

IN THE

# Supreme Court of the United States

BP AMERICA PRODUCTION COMPANY AND
ATLANTIC RICHFIELD COMPANY,
*Petitioners,*

v.

REJANE BURTON,
ACTING ASSISTANT SECRETARY OF THE INTERIOR
FOR LAND AND MINERALS MANAGEMENT, *et al.*,
*Respondents.*

**On Writ of Certiorari**
**to the United States Court of Appeals**
**for the District of Columbia Circuit**

## REPLY BRIEF FOR PETITIONERS


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## REPLY BRIEF FOR PETITIONERS

The government in essence argues that the phrase "[e]very action" in Section 2415(a) does not really mean "every action." Rather, the government urges that the phrase includes *some* actions—adjudicative actions before a *court*—but excludes others—adjudicative actions before an *agency*. That argument contravenes not only the statute's "patently broad" text, *OXY USA, Inc.* v. *Babbitt*, 268 F.3d 1001, 1005 (10th Cir. 2001) (*en banc*), but fundamental canons of construction as well. It renders an entire subsection of the statute—Section 2415(i)'s exception for administrative offsets—superfluous. It is at war with Section 2415's structure, and destroys Congress's careful calibration of record-retention and limitations periods.

More important, that construction would all but deprive Section 2415(a) of practical effect. In the government's view, Section 2415(a) limits the time to pursue claims in court in the first instance, but permits the very same claims to be pursued administratively in perpetuity *and* in court thereafter within one year of final administrative decision. That eliminates both the repose and the incentive for diligent prosecution that Section 2415(a) was supposed to provide. Courts should not "rewrite a statute in hopes of better achieving one of Congress's purposes." Gov't Br. 40-41. But nor should they disregard a textually proper construction in favor of one that is so crabbed that it not only subverts the statutory purpose, but also converts the statute into a virtually meaningless gesture.

The government's reliance on "strict construction" is misplaced. Even when strictly construing a limitations period, this Court must give effect to statutory text; avoid rendering provisions superfluous; and ensure that it does not undermine the statute's intended effect. Just like the construction this Court rejected in *Bowers* v. *New York & Albany Lighterage Co.*, 273 U.S. 346 (1927), the government's construction here would contravene each of those requirements.

### A. The Terms "Action" And "Complaint" Encompass Administrative Adjudications

Section 2415(a)'s breadth is evident from its text: It applies to "every action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract." 28 U.S.C. § 2415(a).

1. The government does not deny that, in modern usage, the word "action" is sufficiently broad to encompass both judicial and administrative actions for money, such as the one at issue here.[1] Nor does it dispute that dozens of statutes and regulations use the term "action" in precisely that fashion. Pet. Br. 19-23 & nn. 3-7; Gov't Br. 20. Nonetheless, the government asserts that the words "every action," when used by themselves, do not encompass administrative actions. Noting the many statutes and regulations that use phrases like "administrative or civil action," the government asserts that, when Congress "intends a phrase that includes the word 'action' to govern administrative proceedings, it says so expressly." Gov't Br. 20-21.

That position is unfounded. Congress and agencies often use the word "action" by itself to encompass administrative and judicial actions alike; context then *proves* that the word "action" is used in that sense. For example, the FDCA authorizes an "[a]ction by the Secretary" for money penalties before the agency and, in the alternative, an "[a]ction by the Attorney General" in court. 21 U.S.C. § 335b(b)(1)(A), (B). It then limits *both* by declaring that "*[n]o action* may be initiated under this section" more than 6 years after the facts become known to the government or 10 years after the events take place. *Id.* § 335b(b)(3) (emphasis added); see also 31 C.F.R. § 501.703(b) (declaring that agency rules for adjudication must be construed to promote "just, speedy, and inexpensive determination of every action"). The MMS itself, in formal orders, often uses the word "action" without

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[1] The government declines to contest in this Court that the instant action is "for money damages" and is "founded upon [a] contract." See Pet. Br. 45-50; Gov't Br. 41 n. 14; contrast Br. in Opp. 18-19.

elaboration to encompass adversary administrative actions, including the action to recover royalties at issue here. See Pet. Br. 21 & n.8; Gov't Br. 21 n.4. That ordinary usage by the relevant agency is surely probative of ordinary meaning. The government's argument, moreover, is based on heads-I-win, tails-you-lose illogic.[2] It is also backwards: Where Congress wishes to *exclude* administrative actions, it does so expressly, using modifiers unique to the judicial process. Pet. Br. 24-25 & nn.12-14 (citing examples). The absence of such limiting language here speaks volumes.

Besides, the fact that the word "action" is regularly used to encompass administrative proceedings—even in phrases such as "civil or administrative action" or "action or proceeding before a[n] * * * administrative agency," Pet. Br. 19-21 & nn.3-7—makes clear that "administrative actions" are a subset of the more general category "actions." If, as the government posits, the term "action" excluded administrative actions, putting the word "administrative" in front of "action" could not expand its scope. Here, moreover, Congress did not need the word "administrative" to make Section 2415's all-encompassing scope clear. Congress declared that Section 2415(a) applies to "*every* action." It is nonsensical to argue that, because Congress and regulators identify "administrative actions" as a subset of "actions" in many contexts, administrative actions are not encompassed within the phrase "*every* action" in Section 2415(a).[3]

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[2] The government demands proof that Congress and agencies use the word "action" to encompass administrative actions. But, when confronted with myriad statutes and regulations that do precisely that, see Pet. Br. 18-21, the government rejects them because context, definitions, or modifiers make it *clear* that Congress used "actions" to encompass administrative actions. If we cited statutes or regulations lacking those features, the government would of course dismiss those as ambiguous.

[3] The government also argues that Section 2415 should be limited to judicial proceedings because "Section 2415 is located within Title 28" of the U.S. Code, "which is entitled 'Judiciary and Judicial Procedure'—not 'Administrative Procedure.'" Gov't Br. 24. But Section 2415 belongs in Title 28 because it governs *both* judicial and administrative actions. Title

2. The government likewise errs in asserting (Br. 16) that the word "complaint" forecloses Section 2415(a)'s application to actions before agencies. The government does not dispute that such actions are often initiated by "complaint." Gov't Br. 21. Instead, it argues that Congress meant to exclude administrative actions because agency "procedures vary substantially," with some employing "different terminology tailored to specific contexts." *Ibid.* But that is backwards: Congress used the broad, generic term "complaint" in Section 2415(a) to refer to any document that *commences* proceedings by "stat[ing] * * * the basis for the plaintiff's claim, and the demand for relief." *Black's Law Dictionary* 303 (8th ed. 2004). As one regulation explains, "[c]omplaint means any document initiating an adjudicatory proceeding, whether designated a complaint * * * or otherwise." 17 C.F.R. § 10.2(f). The government concedes that the term "complaint" includes not only instruments bearing that formal label but also any "functionally similar document." Gov't Br. 21. Not all adjudications begin with a document labeled "complaint." But they all begin with a document that is "functionally similar."

No less than agencies, courts use a variety of terms for what is often referred to as a complaint. In Oklahoma, it is denominated a "petition"; at common law, it was called a "declaration." See Pet. Br. 24 n.11. Yet no one would argue that a federal limitations period regulating when a "complaint" asserting a federal claim must be filed is without effect in Oklahoma courts simply because proceedings in those courts are commenced by "petition." *Ibid.* Likewise here, the fact that some administrative agencies use "different terminology" for the complaint—referring to the submission of a "claim," for example, Gov't Br. 22 (quoting 41

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28 includes other provisions applicable to both judicial and administrative procedure. For example, the Federal Tort Claims Act, codified in Title 28, sets forth procedures for the "[a]dministrative adjustment of claims" against the United States. See 28 U.S.C. § 2672.

U.S.C. § 602 and 42 U.S.C. § 9612(d))—cannot mean that Section 2415(a) lacks application to agency actions.

For the same reasons, the government errs in asserting that, "even if some administrative pleadings were governed by the limitations period, MMS's orders would not be," because "[t]here is no 'complaint' in [MMS's] scheme." Gov't Br. 22, 24. The government argues that the MMS order to pay that began these proceedings does not function as a complaint because "[a] complaint seeks relief," while "an order imposes it." *Id.* at 23. But an MMS order to pay does not fall within the traditional understanding of administrative orders, which are "issued by a government agency *after* an adjudicatory hearing." *Black's Law Dictionary*, *supra*, at 1130 (emphasis added). In MMS practice, the order to pay *precedes* the adjudication, which takes place during the so-called "appeal" under 30 C.F.R. § 290.100, *et seq.* As the Assistant Secretary's sweeping opinion in this case demonstrates, the "appeal" that follows an MMS order to pay is in fact a plenary proceeding to resolve the merits *in the first instance*. See Pet. App. 68a-97a. Both factual and legal issues are adjudicated during the "appeal"; its scope is not constrained by limitations characteristic of appellate review.[4] Thus, while an MMS order may purport to "*command* the payment of royalties," Gov't Br. 23, it (like a complaint) initiates, rather than resolves, MMS's claim.

The contrary position is difficult to reconcile with the Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 ("FOGRSFA"), which established a statute of limitations for oil and gas (but not other minerals) extracted from federal (but not Indian) lands after September 1, 1996. That provision declares that any "judicial proceeding or demand which arises from * * * [a lease] obligation shall be *commenced* within seven years" of when "the obligation

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[4] The government points out that an "informal process" often precedes the issuance of the order. There are no guidelines or regulations governing that process, however, and lessees are not afforded anything resembling an adjudicatory hearing to present a full defense.

becomes due." 30 U.S.C. § 1724(b) (emphasis added). It defines "demand" to include "an order to pay issued by the Secretary" where there is "a reasonable basis to conclude that the obligation in the amount of the demand is due and owing." 30 U.S.C. § 1702(23)(A). FOGRSFA thus recognizes that a so-called MMS "order to pay," far from concluding the action, in fact "*commence[s]*" it. *Id.* § 1724(b). The definition confirms that such orders are not merits dispositions but preliminary "demands" issued if there is a "reasonable basis" (probable cause) to conclude money is owed. *Id.* § 1702(23)(A). Whether money is in fact owed is left for later adjudication. Congress's use of the word "demand" is also telling, since a complaint is a type of "demand." See *Black's Law Dictionary*, *supra*, at 303.

The government's argument also yields absurd results. Under it, an agency can *opt out* of a statutory limitations period by renaming the document that initiates its adjudications. The Mineral Leasing Act does not require that the Department of Interior proceed by "order" or "complaint." Yet, by historical accident, the agency sometimes uses one label and sometimes another. In *Andrus* v. *Shell Oil Co.*, 446 U.S. 657 (1980), for example, the Bureau of Land Management sought to cancel several mineral patents by "issu[ing] administrative *complaints*." *Id.* at 660 (emphasis added). Under the government's theory, the agency could avoid Section 2415's limitations period by renaming all administrative complaints "orders." As noted above (at pp. 4-5, *supra*), the government cannot evade federal limitations periods by filing its lawsuit in a jurisdiction where proceedings are initiated by "petition" or "declaration" rather than "complaint." Likewise, federal agencies cannot avoid the limitations period in Section 2415(a) by choosing to commence proceedings not with a complaint but with an order.

3. This Court's opinions confirm what ordinary usage suggests—that "action" and "complaint" are sufficiently broad to encompass administrative actions like the action for royalties at issue here. Pet. Br. 17-19. Despite the gov-

ernment's protestations, *Pennsylvania* v. *Delaware Valley Citizens' Council for Clean Air*, 478 U.S. 546 (1986), and *West* v. *Gibson*, 527 U.S. 212 (1999), did indeed "construe[] the term 'action' to encompass administrative actions." Gov't Br. 18 (quoting Pet. Br. 17). As this Court later stated, "[i]n *Delaware Valley*, we rejected the contention that the word 'action' * * * should be read narrowly to exclude all proceedings which could be plausibly characterized as 'non-judicial.'" *Sullivan* v. *Hudson*, 490 U.S. 877, 888 (1989).

The government's contrary construction rests largely on the entries for "action" and "complaint" in *Black's Law Dictionary*. See Gov't Br. 9, 14, 15, 16, 17, 23. But this Court is "not bound to accept *Black's* * * * as the authoritative expositor of American Law." *Pioneer Inv. Servs.* v. *Brunswick Assocs.*, 507 U.S. 380, 403 (1993) (O'Connor, J., dissenting). That is particularly true where, as here, the definition does not correspond to current, prevailing usage reflected in court opinions, statutes, regulations, and agency decisions. The cited definition of "action" dates at least to the 1910 second edition (p. 25)—before administrative agencies became commonplace, and well before the APA regularized the trial of adversary actions before them. But the trial of actions before agencies is now common, and *Black's* failure to update an entry cannot turn back the clock.

The government's reliance on *Unexcelled Chemical Corp.* v. *United States*, 345 U.S. 59 (1953), is likewise misplaced. That decision does not "h[o]ld * * * that commencing an 'action' by filing a 'complaint' refers, in its 'ordinary sense,' to filing a complaint in court, not to initiating an administrative proceeding." Gov't Br. 17. The primary question in *Unexcelled* was whether the two-year limitations period in the Portal-to-Portal Act, 29 U.S.C. § 255, applied to a *judicial action* for liquidated damages. The Court held that it did. 345 U.S. at 63-64.

In a single paragraph, *Unexcelled* responded to the government's alternative argument that its suit was filed within the two-year limit. The Portal-to-Portal Act provides that

"'an action is *commenced* for the purposes of [the statute] * * * on the date when the complaint is filed.'" 345 U.S. at 66 (quoting 29 U.S.C. § 256) (emphasis added). The government argued that its suit, although filed after the two-year period, was timely because the action was "commenced" three years earlier, with the Secretary of Labor's "issuance of a formal complaint in the [separate] administrative proceedings." *Ibid.* The Court rejected that argument, stating that "[c]ommencement of an action by the filing of a complaint has too familiar a history and the purpose of §§ 6 and 7 was too obvious for us to assume that Congress did not mean to use the words in their ordinary sense." *Ibid.*

Properly understood, that does not mean that administrative actions were exempt from the statute of limitations. That was not at issue, since the administrative proceedings *were* brought within the two-year period.[5] The question was whether the timely filing of the administrative complaint could be said to "commence" the later, distinct judicial action so as to make it timely. (Unlike Section 2415(a), the Portal-to-Portal Act lacked a relevant provision to toll the limitations period during administrative proceedings.) Invoking the purpose of the provisions at issue, this Court answered that question in the negative, consistent with the "familiar * * * history" that an action is "commenced" when the complaint in *that proceeding* is filed, not when a complaint in some earlier, separate proceeding is filed. 345 U.S. at 66. *Each* action subject to a statute of limitations—administrative or judicial—must be filed within the speci-

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[5] The text of the Portal-to-Portal Act, moreover, made it clear that it was limited to judicial proceedings. The section at issue in *Unexcelled* specifically refers to "the *court* in which the action is brought" and "the *court* in which the action was commenced." Portal-to-Portal Act of 1947, § 7, 61 Stat. 88, currently codified at 29 U.S.C. § 256 (emphasis added). Similarly, the provision of the Walsh-Healy Act at issue allowed liquidated damages in "*suits* brought in the name of the Attorney General." *Unexcelled*, 345 U.S. at 65-66 n.4 (emphasis added). In contrast, Section 2415(a) applies to "every action," and contains no references to "court" or "suit" that might limit its scope. See p. 2, *supra*; Pet. Br. 24-26.

fied period. The *administrative* complaint thus may have "commenced" the *administrative* action. But it could not be said to have commenced the *separate judicial action* so as to make it timely. For that, a complaint had to be filed in court within the limitations period. *Ibid.* That unexceptional ruling sheds no light on the issue before this Court.

**B. The Government's Construction Renders An Entire Subsection Of Section 2415 Superfluous**

To the extent Section 2415(a)'s scope is in doubt, the remainder of the statute erases any question. It is a "'cardinal principle of statutory construction' that 'a statute ought, upon the whole, to be so construed that, if it can be prevented, no clause, sentence, or word shall be superfluous, void, or insignificant.'" *TRW Inc.* v. *Andrews*, 534 U.S. 19, 31 (2001) (quoting *Duncan* v. *Walker*, 533 U.S. 167, 174 (2001)). In this case, Subsection (i) of Section 2415 expressly exempts "administrative offsets" from the limitations period that Section 2415(a) otherwise establishes. That exception for administrative offsets would be entirely unnecessary if the limitations period did not apply to administrative proceedings in the first place. Pet. Br. 26-30. Court after court, including the D.C. Circuit, has acknowledged as much. Pet. App. 18a; *OXY*, 268 F.3d at 1006; *United States* v. *Hanover Ins. Co.*, 82 F.3d 1052, 1055 (Fed. Cir. 1996).

To evade that "cardinal principle," the government invokes legislative history, urging that Congress added Subsection (i) merely "to 'clarify[]' that the limitations period does not apply to administrative offsets." Gov't Br. 31. Even if isolated references to "clarification" in a Senate Report, Gov't Br. 31 (quoting Sen. Rep. No. 378, 97th Cong., 2d Sess. 2, 16 (1982)), could trump the rule against superfluity—and they cannot—the Senate Report's substance is to the contrary. The Report begins by observing that "[Subsection (i)] *allows* collection of delinquent debt owed the government by administrative offset beyond the six-year statute of limitations." Sen. Rep. No. 378, *supra*, at 16 (emphasis added). It explains that "[t]he Justice Depart-

ment has determined that *the six-year statute of limitations prevents the government from collecting debts by means of offset*, thus, the government will be unable to collect a just debt from many debtors *because the statute of limitations has run out*." *Ibid.* (emphasis added); see *id.* at 16-17 (noting the need to amend because, under the then-existing version of Section 2415, "if more than six years passes * * *, the government will be unable to set off the employee's retirement pay"). Finally, it summarized that "[t]his *revision* to Section 2415 *would allow* administrative offset of delinquent debts owed the government * * * beyond the six-year statute of limitations." *Id.* at 17 (emphasis added). That such a "revision" was thought necessary to "allow" the pursuit of administrative offsets "beyond the six-year statute of limitations," *id.* at 16-17, shows that Subsection (i) had the substantive effect of affirmatively excepting administrative offsets from an otherwise applicable limitations period.

The government also urges that excluding administrative actions from Section 2415(a) would not convert the administrative-offset exception into surplusage:

> If the debt * * * could otherwise be enforced only through an affirmative action in court, and an action in court on that debt would be barred by Section 2415(a), Section 2415(i) clarifies that such an offset is not time-barred. The question whether an otherwise time-barred claim can be used defensively as an offset in that manner arises whether or not Section 2415(a) limits only court actions or both court actions and administrative proceedings brought by the government.

Gov't Br. 32. That argument, to the extent it makes sense, contradicts the government's observation that "a statute of limitations extinguishes only the remedy, not the underlying right." Gov't Br. 13 (citing *Beach* v. *Ocwen Fed. Bank*, 523 U.S. 410, 416-417 (1998)). If Section 2415(a) barred *only* actions *in court*, it would be perfectly clear that agen-

cies could pursue otherwise barred claims by *administrative* offset even absent Section 2415(i)'s exception.[6]

The government likewise errs when it dismisses Section 2415(i)'s relevance by urging that "'[t]he views of a subsequent Congress form a hazardous basis for inferring the intent of an earlier one.'" Gov't Br. 30 (quoting *Mackey* v. *Lanier Collection Agency & Serv., Inc.*, 486 U.S. 825, 840 (1988)). To the contrary, even where a provision is added by amendment, this Court interprets the resulting statute as if it had read that way from the outset. *United States* v. *LaFranca*, 282 U.S. 568, 576 (1931); Pet. Br. 30 (citing additional authority). It thus is not our view that Subsection (i) "expand[ed] the statute's coverage to other administrative proceedings." Gov't Br. 30; see also *id.* at 11, 33. It is that, regardless of how one might read Section 2415(a) in isolation, the statute as a whole—including Subsection (i)—makes it clear that Section 2415(a) extends to administrative actions except where, as in Section 2415(i) itself, Congress provides otherwise.

### C. Excluding Administrative Proceedings From Section 2415(a) Renders Its Effects Illusory

The government, moreover, largely ignores one of the most fundamental defects in its construction—that it deprives Section 2415(a) of practical effect.

1. The government urges that, even if judicial actions founded on contract are barred by the limitations period, it may pursue precisely the same claims administratively in perpetuity. But that converts Section 2415(a) into a meaningless gesture. Section 2415's primary purpose is to provide the repose Congress thought "required by modern standards of fairness and equity." Sen. Rep. No. 1328, 89th Cong., 2d Sess. 2 (1966); see Pet. Br. 35-37. Under the

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[6] Indeed, once the government took such an administrative offset, the claimant could sue for any money withheld as a result. The government then could assert its claim as an offset *in that judicial action* without regard to the limitations period. See 28 U.S.C. § 2415(e). The government's construction thus makes Section 2415(i) doubly superfluous.

government's theory, however, Section 2415(a) would protect against actions in court after six years, but leave individuals exposed to the same liabilities for the same claims before the agency in perpetuity. That is no repose at all. Worse still, the individual could also be liable for decades of interest, based on a disputable "clarification." See Pet. Br. 38-40. As the Office of Legal Counsel observed when interpreting Section 2415(a), "if the United States could administratively collect time-barred debts where no claim was filed against it, this would result in a completely ineffective statute of limitations" and "the repose intended by § 2415 would be illusory." *Effect of Statute of Limitations on Administrative Collection of United States Claims*, Mem. Op. Off. of Legal Counsel 7-8 (Sept. 29, 1978).

Far from denying that result, the government embraces it—and urges that it can bring judicial actions in perpetuity as well. According to the government, "administrative proceedings * * * *trigger* the limitations period; they are not 'actions' governed by it." Gov't Br. 15 (emphasis added). The government thus does not merely claim that it can collect contract damages at any point in the future through an administrative action. It also claims that it can wait until the limitations period expires, file an administrative action, and *then* file a judicial action one year after the administrative action terminates. The government thus argues that, despite the six-year limitations period, it has forever to bring administrative actions, and forever plus a year to file in court. "It is an elementary rule of construction that 'the act cannot be held to destroy itself.'" *Citizens Bank of Md.* v. *Strumpf*, 516 U.S. 16, 20 (1995) (quoting *Tex. & Pac. Ry. Co.* v. *Abilene Cotton Oil Co.*, 204 U.S. 426, 446 (1907)). Yet that is precisely the effect of the government's construction.

2. The government's construction also destroys the other "salutary effect[s]" Congress intended Section 2415(a) to have. Pet. Br. 4 (quoting Sen. Rep. No. 1328, *supra*, at 2). A statute of limitations increases governmental efficiency by forcing agencies to pursue claims "at a

sufficiently early time so that necessary witnesses, documents, and other evidence are still available * * * ." Sen. Rep. No. 1328, *supra*, at 12. It avoids "judicial hostility to old claims" and "minimizes * * * collection problems arising with respect to debtors who have died, disappeared, or gone bankrupt." *Ibid.* If agencies know they can recover administratively indefinitely—with interest—any incentive for prompt prosecution is lost. Thus, while *amici* stress that Indian Tribes "rely on MMS to perform its royalty enforcement duty consistent with the United States' trust responsibility," Br. *Amici* Jicarilla Apache Nation, *et al.* 26-27 ("Jicarilla Br."), Congress determined that the government performs that duty best when confronted with the discipline provided by an enforceable limitations period.

Implicitly acknowledging that its construction defeats Section 2415(a)'s purposes, the government asserts that appeals to "general policies of fairness and repose" cannot overcome statutory text. Gov't Br. 35 (quoting Pet. App. 20a). But the issue is not policy. It is statutory meaning. The government asks this Court to reject a proper textual construction adopted by two courts of appeals in favor of one that defeats every single one of Congress's stated purposes in enacting the statute. The rules of construction will not tolerate that result. See *Griffin* v. *Oceanic Contrs. Inc.*, 458 U.S. 564, 575 (1982) ("absurd results are to be avoided" where "alternative interpretations consistent with the legislative purpose are available"); *Neder* v. *United States*, 527 U.S. 1, 15 (1999) (Court is "entitled to stand back and see" the practical impact of its decisions).

For related reasons, the government's claim that "[p]etitioners mostly avoid Section 2415(a)'s legislative history," Gov't Br. 29, is misdirected. That history—which carefully documents each purpose underlying Section 2415(a)—is discussed in detail in our opening brief. Pet. Br. 3-4, 35-38. And, as we explained, the government's construction is at

war with each purpose identified in the legislative history. *Id.* at 35-38. On that issue, little more need be said.[7]

3. The government's construction, moreover, wreaks havoc with Section 2415's structure. Throughout Section 2415, Congress established stricter limits for the offensive assertion of government claims (claims to extract money from others) than for their defensive assertion (to avoid paying money) by an offset or otherwise. Pet. Br. 31-32. The government's construction, however, would set that careful structure on its head. Under it, offensive judicial actions to extract money would be subject to a six-year limitations period, 28 U.S.C. § 2415(a); administrative offsets to withhold money otherwise payable would be subject to a longer 10-year statute of limitations, 31 U.S.C. § 3716(e)(1) (expressly referenced in 28 U.S.C. § 2415(i)); but offensive administrative actions to extract money would be subject to no limitations period whatsoever. See Pet. Br. 31-32. The government never explains why Congress would have adopted that irrational structure.[8]

The government's construction also destroys the congruence that Congress, on two separate occasions, established between the limitations period and the record-retention period for oil and gas lessees. See Pet. Br. 32-33. The gov-

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[7] Rather than examine the legislative history, the government cherry-picks references to "suits" or "civil actions." Gov't Br. 27-29. Those references prove that Congress understood Section 2415(a) to cover judicial actions, but they do not prove that Congress meant to exclude administrative actions; nor does anything else. In any event, to the extent legislative history is relevant, it must give courts an understanding of the problem Congress confronted and the legislation's purposes. The government's position cannot be reconciled with either.

[8] The government hypothesizes that "affirmative administrative actions" sometimes "*may* be limited by context-specific limitations periods." Gov't Br. 33 n.9 (emphasis added). But Section 2415(a) was designed as a catch-all for situations in which Congress has not enacted context-specific limitations periods—it applies "*except* as otherwise provided." 28 U.S.C. § 2415(a) (emphasis added). The government never explains why that structure is rational in a catch-all either.

ernment does not dispute that its construction has that effect. Instead, it dismisses the notion that lessees will feel bound to retain pre-1996 records in perpetuity, asserting that "the lawful destruction of records would make the issuance of an order to pay unlikely." Gov't Br. 40. That attempted reassurance provides little comfort where, as here, liability can run into the tens or hundreds of millions of dollars; where, as here, the government claims the ability to detect underpayments well into the past; and where, as here, older claims are *more* valuable to the government because it can collect decades of interest. Pet. Br. 38-40.[9] The government's effort at reassurance, in any event, is hardly license to adopt a construction that destroys the coherence and symmetry of the statutory scheme—including the matching of record retention obligations and limitations periods—that Congress intended.

Finally, the government's construction destroys the symmetry Section 2415 sought to establish between the government and private litigants. Section 2415 is "a statute aimed at equalizing the litigative opportunities between the Government and private parties." *Crown Coat Front Co.* v. *United States*, 386 U.S. 503, 521 (1967). Yet the government would construe Section 2415(a) to give private entities six years to bring their claims, 28 U.S.C. § 2401; 41 U.S.C. § 605(a), while giving the government forever to bring its claims administratively. The government argues that symmetry "has little application to administrative proceedings that only the agency can initiate, and in which the agency is charged with interpreting then-governing statutes and regulations." Gov't Br. 36. That might be true for genuine "regulatory" proceedings, such as rulemakings or discipli-

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[9] MMS retains certain reports on royalties "indefinitely," Jicarilla Br. 14 n.9, and the government itself asserts that "audits can detect systematic underpayment dating back more than six years," Gov't Br. 37. Of course, what the government calls a "systemic underpayment" may merely result from MMS's after-the-fact "clarification" of how it interprets its rules. See Pet. Br. 39-40.

nary proceedings. But Section 2415 addresses "action[s] for money damages * * * founded upon * * * contract." 28 U.S.C. § 2415(a). When the government pursues an action for money damages, its claims "are almost indistinguishable from claims made by private litigants." Sen. Rep. No. 1328, *supra*, at 2. Yet the government would destroy the symmetry between private parties and the government that Congress sought to establish.

**D. The Canon Of "Strict Construction" Does Not Counsel A Contrary Result**

Ultimately, the government concedes that "the statutory terms 'action' and 'complaint' are sometimes used to refer to administrative proceedings." Gov't Br. 18. It urges, however, that "the canon requiring strict construction of limitations periods against the government counsels against giving those terms a broader reading here." *Ibid.* But "strict construction" does not require this Court to ignore the inherent breadth of a statutory term:

> "The rule of strict construction is not violated by permitting the words of the statute to have their full meaning, or the more extended of two meanings * * *; but the words should be taken in such a sense, bent neither one way nor the other, as will best manifest the legislative intent."

*SEC* v. *C.M. Joiner Leasing Corp.*, 320 U.S. 344, 355 (1943) (quoting *United States* v. *Hartwell*, 73 U.S. (6 Wall.) 385, 396 (1867)). "[S]trict construction" simply means that the scope of a statute cannot be "enlarged * * * beyond what the language requires." *United States* v. *Nordic Village, Inc.*, 503 U.S. 30, 34 (1992).

This Court has for that reason rejected strict construction arguments in circumstances nearly indistinguishable from those here. In *Bowers* v. *New York & Albany Lighterage Co.*, 273 U.S. 346 (1927), the Court addressed whether a statute of limitations barring the United States from initiating a "suit or proceeding for the collection of * * * taxes" after five years applied to the government's use of the

administrative procedure of "distraint." *Id.* at 348 & n.1. The government argued that the statute of limitations did not apply to distraint because "the word 'proceeding' refers only to a proceeding in court." *Id.* at 349. The government also asserted that, under the canon of "strict construction," "any ambiguity in the clause under consideration must be resolved in [its] favor." *Ibid.*

The Court agreed that it was required to apply a strict construction, but rejected the government's reading. The Court observed that the language at issue was sufficiently broad "and commonly used to comprehend steps taken in" both "judicial proceeding[s]" and "executive proceeding[s]." 273 U.S. at 349. The Court further noted that the government's reading of the statute was "inconsistent" with statutory text because it would render another provision of the statute superfluous. *Id.* at 351. And finally, the Court noted that, even in the context of "strict construction," it was required to examine "the terms and purpose of the statute":

> The purpose of the enactment was to fix a time beyond which * * * collection might not be initiated. The repose intended would not be attained if suits only were barred, leaving the collector free at any time to proceed by distraint. * * * The mischiefs to be remedied by setting a time limit against distraint are the same as those eliminated by bar against suit.

*Id.* at 349. Accordingly, the Court held that "the meaning of 'proceeding' * * * cannot be restricted to steps taken in a suit; it includes as well steps taken for collection of taxes by distraint." *Id.* at 352.

Each of the reasons the Court gave for rejecting the government's argument in *Bowers* applies with equal force here. Here, as in *Bowers*, the relevant terms are commonly used in reference to both administrative and judicial actions. Here, as in *Bowers*, the government's proposed construction would render a provision of the statute superfluous. And here, as in *Bowers*, excluding administrative proceedings from the scope of the statute of limitations

would completely undermine Congress's purpose in enacting the statute, which was to provide repose. Simply recognizing that the text and purpose of Section 2415 encompass administrative proceedings in addition to judicial proceedings does not violate the canon of "strict construction."

**E. Amendments To The Mineral Leasing Act Do Not Support the Government's View**

1. The government and its *amici* also argue that two amendments to the Mineral Leasing Act ("MLA")—FOGRMA in 1982 and FOGRSFA in 1996—"[d]emonstrate that Section 2415(a) [d]oes not [a]pply to MMS [o]rders to [p]ay [r]oyalties." Jicarilla Br. 11; Gov't Br. 36-39. They first assert that FOGRMA "was intended to provide [] more rigorous enforcement," Jicarilla Br. 12, and directed MMS to "audit and reconcile, to the extent practicable, all current and past leases of oil or gas and take appropriate actions." 30 U.S.C. § 1711(c)(1); Gov't Br. 36. They thus assert that FOGRMA "hardly manifests an intent to limit liability." Gov't Br. 36. But amendment of the MLA to provide more "rigorous enforcement" in 1982 provides no insight into the scope of a general statute of limitations enacted in 1966.

FOGRMA does not address Section 2415(a), or the limitations period for administrative actions for royalties.[10] Where the "later law[] * * * 'do[es] not seek to clarify an earlier enacted general term' and 'do[es] not depend for [its] effectiveness upon clarification * * * of an earlier statute,'" that later law is "'beside the point' in reading the first enactment." *Gutierrez* v. *Ada*, 528 U.S. 250, 257-258 (2000). The direction to the MMS to "audit and reconcile" accounts, moreover, is limited by the phrase "to the extent practicable." It hardly licenses MMS to bring stale actions that, because of a time bar, are clearly impracticable.

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[10] Both the government and *amici* note that FOGRMA established a limitations period for penalties, 30 U.S.C. § 1755, but not "orders directing a lessee to pay past-due royalties." Gov't Br. 37 n.11; see Jicarilla Br. 13. But that shows that Congress saw no need to address royalty payments, which were already covered by Section 2415(a).

The government's concerns about "rigorous enforcement" boil down to the complaint that six years is not enough time because it must conduct audits before commencing actions. Gov't Br. 38-39. That assertion, better addressed to Congress, is meritless. Six years is a generous period; when Congress enacted a prospective limitations period for certain MMS actions in FOGRSFA, it gave the government just one more year, for a total of seven. 30 U.S.C. § 1724(b)(1). That belies the government's current claim that "rigorous enforcement" requires it to have infinite time. Infinite time horizons are, in any event, the enemy of rigorous enforcement, because they give the government no reason to proceed with appropriate diligence.

2. The Jicarilla Tribe also argues that FOGRSFA's amendment to the Mineral Leasing Act to create a prospective limitations period for certain MMS orders "indicates that Congress in 1996 did not understand the general statute of limitations in Section 2415(a) to apply to MMS administrative orders." Jicarilla Br. 15; see p. 5-6, *supra*. That inference is unfounded. When Congress enacted that provision, the courts were divided on whether Section 2415(a) applied to administrative actions.[11] By acting prospectively, Congress at most declined to resolve that dispute.

Far from agreeing with the MMS and those courts that held Section 2415(a) to be inapplicable, Congress found "serious problems with the way" those "courts and consequently the MMS have interpreted the time within which collection of amounts due * * * can be undertaken." *Feder-*

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[11] Contrast *Hanover Ins. Co.*, 82 F.3d at 1055 ("Section 2415(a) applies to administrative actions"), and *Glenn Elec. Co.* v. *Donovan*, 755 F.2d 1028, 1031 (3d Cir. 1985) (observing that the district court's "well-reasoned opinion" had held that "the proper limitation period" for the administrative actions "was the general six-year period prescribed in 28 U.S.C. § 2415(a)"), with *Phillips Petroleum Co.* v. *Johnson*, No. 93-1377, 1994 WL 484506 (5th Cir. Sept. 7, 1994) (limitations period inapplicable to administrative action), and *Samedan Oil Corp.* v. *Deer*, No. Civ. A. 94-2123, 1995 WL 431307 (D.D.C. June 14, 1995) (same).

*al Oil & Gas Royalty Simplification and Fairness Act of 1995: Report of the S. Comm. on Energy and Natural Res.*, 104th Cong., 2d Sess. 14 (1995). Cases like *Samedan* and *Phillips*, which "held no statute of limitations applies," Congress declared, "compel enactment" of a new limitations period. *Seven-Year Balanced Budget Reconciliation Act of 1995: Report of the House Comm. on the Budget*, 104th Cong., 1st Sess. 571 (1995). That Congress enacted a prospective limitations period for oil and gas leases to rectify the "serious problems" created by court and MMS decisions hardly suggests that Congress agreed with those decisions.

Congress's decision to act prospectively, moreover, is consistent with the expectation that this Court would eventually hold that Section 2415(a) does apply here. By acting prospectively, Congress avoided the constitutional issues that arise when a new, longer limitations period is enacted and made applicable to claims that, under the prior limitations period, were already barred. See, *e.g.*, *In re Enter. Mortgage Acceptance Co. Sec. Litig.*, 391 F. 3d 401, 410 (2d Cir. 2005) (holding that "the resurrection of previously time-barred claims" is "impermissibl[y] retroactive"). Besides, where there is no limitations period for past claims, Congress generally makes the new statute of limitations applicable to those claims too, while protecting claimholders by deeming such claims to have accrued on the day the new statute of limitations is enacted. That is precisely what Congress did when it enacted Section 2415(a). Pet. Br. 6, 44. That Congress did not do likewise in FOGRMA is evidence that such claims were already subject to a limitations period—not that Congress intended those claims (but not later-accruing claims) to persist in perpetuity.

* * * * *

For the foregoing reasons and those set forth in petitioner's opening brief, the judgment of the D.C. Circuit should be reversed.

Respectfully submitted.

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IN THE

# Supreme Court of the United States

BP AMERICA PRODUCTION COMPANY, SUCCESSOR IN INTEREST TO AMOCO PRODUCTION COMPANY, *et al.*,

*Petitioners*,

*v.*

REBECCA W. WATSON, ASSISTANT SECRETARY, LAND AND MINERALS MANAGEMENT, DEPARTMENT OF THE INTERIOR, *et al.*,

*Respondents.*

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

## BRIEF OF AMICUS CURIAE. THE AMERICAN PETROLEUM INSTITUTE, SUGGESTING REVERSAL

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## I. INTEREST OF AMICUS CURIAE

The American Petroleum Institute ("API") submits this amicus brief in support of Petitioner, BP America Production Company ("BP"), to address an issue that is critical to the federal oil and gas leasing program: to wit, whether the Department of the Interior ("Interior"), after having taken no action whatsoever for more than six years, can initiate legal proceedings to collect lease royalties notwithstanding the six-year statute of limitations that bars "every action for money damages brought by the United States or an officer or agency thereof which is founded upon contract." 28 U.S.C. § 2415(a).[1] Interior contends that the statute has no application where the agency initiates its collection action by issuing an administrative royalty payment order. Thus, according to Interior, the United States has *carte blanche* to assert claims for additional royalties going back forever. Interior's position is more than patently unfair – it is erroneous as a matter of law.

API is a non-profit, nationwide trade association that represents over four hundred companies engaged in all aspects of the oil and gas industry, including exploration and production, refining, marketing and transportation. API members and hundreds of other companies and individuals own oil and gas leases administered by Interior covering millions of acres of federal and Indian lands. Pursuant to its

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1. The parties have consented to the filing of this brief. Counsel for a party did not author this brief in whole or in part. No person or entity, other than the Amicus Curiae, its members, or counsel made a monetary contribution to the preparation and submission of this brief. Although Petitioner is a member of API, Petitioner did not make a monetary contribution to the preparation and submission of this brief.

statutory mandate to undertake "enforcement practices that ensure the prompt and proper collection and disbursement of oil and gas revenues," 30 U.S.C. § 1701(b)(3), Interior issues administrative orders directing federal and Indian lessees to pay additional royalties. In contrast to a private mineral lessor's written request for payment of royalties, Interior's royalty payment orders carry the heavy weight of federal law. An order issued by Interior exposes a lessee to civil and criminal penalties, and the lessee's failure to satisfy jurisdictional appeal requirements waives any and all defenses to Interior's claim. Since the enactment in 1982 of the Federal Oil and Gas Royalty Management Act, 30 U.S.C. § 1701 *et seq.* ("FOGRMA"), Interior has issued numerous orders to pay additional royalties, each one of which has placed a lessee's rights in jeopardy.

In hundreds of administrative appeals, API members have asserted that Interior's royalty payment orders were barred by the six-year limitations period. In every case, Interior rejected the lessee's defense on the grounds that "statutes of limitations apply to judicial enforcement of administrative actions, but not to the underlying administrative actions." *Anadarko Petroleum Corp.*, 122 IBLA 141, 147 (1992). Then, Interior's typical practice has been to render a final administrative decision ordering the lessee to pay additional royalties, which forces the lessee either (1) to file suit for judicial review of Interior's administrative decision, or (2) to risk incurring penalties by electing not to comply with Interior's decision, in an effort to cause Interior to file suit to enforce its decision, at which time the lessee would reassert the statute of limitations defense. However, mindful that Interior can impose significant penalties upon a lessee who does not comply with a Departmental order to pay, *see Marathon Oil Co.*, 106 IBLA

104 (1988), lessees have not been willing to assume the risks attendant with refusing to comply with an Interior decision. As a result, federal court litigation over Interior's late-asserted royalty claims has been filed by lessees rather than by Interior. Once in court, Interior has consistently argued that, because the matter is not a "judicial enforcement proceeding" filed by the United States, the statute of limitations still does not apply. Reviewing this precise sequence of events – which has played out repeatedly in cases involving API members – the Court of Appeals for the District of Columbia Circuit agreed with Interior.

API respectfully urges the Court to reverse the decision below by the D.C. Circuit and to adopt the opposing analysis that the Court of Appeals for the Tenth Circuit applied in *OXY USA, Inc. v. Babbitt*, 268 F.3d 1001 (10th Cir. 2001). The result advocated by Interior and accepted by the D.C. Circuit contradicts the clear language of 28 U.S.C. § 2415, it defeats Congress's intent to close stale contractual claims and "equaliz[e] the litigative opportunities between the Government and private parties," *Crown Coat Front Co. v. United States*, 386 U.S. 503, 521 (1967), and it undermines the established principle that statutes of limitation are "fundamental to a well-ordered judicial system." *Board of Regents v. Tomanio*, 446 U.S. 478, 487 (1980).

## II. STATEMENT OF THE CASE

### A. API's Experience With Interior's Royalty Collection Program

On behalf of the United States, Interior administers oil and gas leases granted pursuant to the various federal leasing statutes, including, *inter alia*, the Mineral Leasing Act, 30 U.S.C. § 181 *et seq.*, and the Outer Continental Shelf Lands Act, 43 U.S.C. § 1331 *et seq.* Federal and Indian oil and gas leases (whether onshore or offshore) generally obligate the lessee to pay royalties monthly as oil and gas is produced. 30 C.F.R. § 218.50. The amount of royalties paid is determined by the royalty fraction established in the lease, multiplied by the "value of production." *See, e.g.*, 30 C.F.R. § 206.100 *et seq.* Federal and Indian lessees pay the United States billions of dollars in royalties each year and report millions of lines of data on their monthly royalty reports. Due to a variety of factors – including the complexities of royalty accounting, uncertainties inherent in determining the "value of production," disruptions in the economy, and changes in federal regulation – federal courts are frequently called upon to resolve disputes concerning the amount of royalties that a federal or Indian lessee must pay.[2]

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2. *See, e.g., Fina Oil & Chem. Co. v. Norton*, 332 F.3d 672 (D.C. Cir. 2003); *Amerada Hess Corp. v. DOI*, 170 F.3d 1032 (10th Cir. 1999); *In re Century Offshore Mgmt. Corp.*, 111 F.3d 443 (6th Cir. 1997); *Shell Oil Co. v. Babbitt*, 125 F.3d 172 (3d Cir. 1997); *Chevron U.S.A., Inc. v. United States*, 923 F.2d 830 (Fed. Cir. 1991); *Diamond Shamrock Exploration Co. v. Hodel*, 853 F.2d 1159 (5th Cir. 1988); *Marathon Oil Co. v. United States*, 807 F.2d 759 (9th Cir. 1986).

In 1982, Congress passed FOGRMA, which gave Interior extensive investigatory and enforcement powers relating to the collection of royalties from federal and Indian lessees. *See* 30 U.S.C. §§ 1717-1722. As a result, many of API's members house "resident auditors" from Interior's subagency, the Minerals Management Service ("MMS"), who work full time in the lessee's offices conducting royalty audits on behalf of the United States. Using its extensive access to lessee accounting data, MMS verifies the correctness of a lessee's royalty accounting (which is accurate in most cases), and notifies the lessee of findings of payment errors. Based on these audits, MMS issues royalty payment orders to federal and Indian lessees.

MMS's issuance of a royalty payment order immediately and irretrievably places a lessee's legal rights in jeopardy. First, every MMS royalty payment order threatens the lessee with the imposition of penalties for noncompliance. *See* 30 U.S.C. §§ 1719-1720; 30 C.F.R. Part 241; *Marathon Oil Co.*, 106 IBLA 104 (1988). Moreover, although MMS's royalty payment orders are frequently erroneous, the right to assert legal and factual defenses will be waived if the lessee does not file an administrative appeal to the Director of MMS within thirty days after receiving MMS's order. *See* 30 C.F.R. Part 290 (Subpart B); *Santa Fe Energy Co.*, 110 IBLA 209 (1989) (holding that failure to appeal timely waives defenses). If the MMS Director rejects the lessee's appeal (which happens in virtually all cases), the lessee must then exhaust its administrative remedies by appealing the MMS Director's decision to the Interior Board of Land Appeals ("IBLA") pursuant to 43 C.F.R. Part 4. Following proceedings before the IBLA, the IBLA issues Interior's "final" administrative decision. On occasion (as in this case), Interior's Assistant Secretary for Land and Minerals Management takes over

jurisdiction of the appeal and issues Interior's final decision. If Interior's final decision rejects the lessee's appeal of MMS's royalty payment order (which happens in most cases), the lessee then may seek judicial review in federal district court.

Critically, Interior does not have to proceed by issuing an administrative order to pay. Rather, like any other mineral lessor, Interior could file suit in federal court asserting the United States' royalty claim. However, because Interior has chosen to initiate administrative proceedings, the normal sequence of events forces the lessee, rather than Interior, to file suit for judicial review in federal court.

### B. The Procedural Catch 22: Interior Refuses To Apply 28 U.S.C. § 2415(a) In Administrative Proceedings, But Never Commences Its Royalty Collection Actions By Filing Suit In Court

Starting in the mid-1980s, and especially in the period 1989-1995, Interior became increasingly aggressive in its royalty collection efforts, with MMS issuing numerous royalty payment orders. Because so many of MMS's orders sought additional royalty payments allegedly owed more than six years before the orders were issued, federal and Indian lessees repeatedly raised 28 U.S.C. § 2415(a) as a defense (in addition to any substantive defenses to Interior's royalty claim). The IBLA's response in *Shell Oil Co.*, 150 IBLA 298 (1999), a case involving one of API's members, is illustrative of the agency's position:

> *28 U.S.C. § 2415*(a) (1994) provides that "every action for money damages brought by the United States * * * which is founded upon any contract

> express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues." We have consistently ruled that statutes establishing time limitations for the commencement of judicial actions for damages on behalf of the United States do not limit administrative proceedings within the U.S. Department of the Interior. *Santa Fe Minerals, Inc., 145 IBLA 317, 323-4 (1998); W.A. Moncrief, Jr., 144 IBLA 13, 15 (1998); Texaco Exploration and Production, Inc., 134 IBLA 267, 270 (1995); Chevron U.S.A., Inc., 129 IBLA 151, 154 (1994).* Moreover, we have specifically declined to rule that MMS demands for additional royalty are barred by that provision. *Marathon Oil Co., 128 IBLA 168, 170-71 (1994); Anadarko Petroleum Corp., 122 IBLA 141, 147-48 (1992).* As we stated in *Alaska Statebank, 111 IBLA 300, 311 (1989)*, a Departmental proceeding requiring payments that accrued more than 6 years before the proceeding was initiated "is not an action for money damages brought by the United States, but rather is administrative action not subject to the statute of limitations."

150 IBLA at 306.

As in many decisions, the IBLA in *Shell Oil Co.* relied on its prior decisions in *Alaska Statebank*, 111 IBLA 300 (1989), and *Anadarko Petroleum Corp.*, 122 IBLA 141 (1992). In both of those cases, the IBLA clearly acknowledged Interior's ability to file a judicial complaint to enforce the government's royalty claims. In *Anadarko* – which Interior relied upon in rejecting Amoco Production Company's

reliance on the statute of limitations in this case – the IBLA stated:

> We are without authority to decide whether the statute of limitation [28 U.S.C. § 2415] would bar a judicial suit to collect royalty deemed owing on a lease; such a determination would be made by the court before which any collection proceeding is brought.

122 IBLA at 147.

In the experience of API's members, Interior's rote deferral of the lessee's statute of limitations defense to "the court before which any collection proceeding is brought" creates a classic "Catch 22," because Interior never initiates a judicial proceeding to collect royalties. Rather, Interior's issuance of a royalty payment order always leads to the lessee filing suit to challenge Interior's final decision upholding its own order. Interior then contends that the lessee's lawsuit is not, in the words of the IBLA, a "judicial suit to collect royalty," but is instead a proceeding for judicial review of final agency action in which the court must defer to the agency ruling. Time and again, API's members have asserted the statute of limitations as a defense to a royalty payment order, only to have Interior side-step the issue.

### C. Amoco Production Company's Appeal

The royalty dispute before this Court is typical of many of the royalty disputes that have arisen between the United States and API's members. In a royalty payment order dated May 27, 1997, MMS asserted that BP's predecessor-in-interest, Amoco Production Company, had improperly

deducted certain post-production costs from the value on which it paid royalty on coalbed methane gas produced during the period January 1989 through December 1996. As is common, the substantive dispute involved a disagreement over the royalty valuation consequences of applying new gas production technologies. And, as in so many other cases, a portion of the royalties that MMS sought to collect were originally due more than six years before MMS issued its order.

## III. SUMMARY OF THE ARGUMENT

The language, structure and legislative history of 28 U.S.C. § 2415 are clear: absent an express exception, the statute imposes a six-year statute of limitations applicable to "every action" in which a federal agency asserts a contract claim, regardless whether such actions are initiated as administrative or judicial proceedings. By holding that Interior's royalty payment order was not time-barred because it was not a "complaint," the D.C. Circuit's decision impermissibly rewrites the language that Congress carefully selected. Restricting "every action" to encompass only judicial proceedings contradicts the text and structure of the statute, and it undermines Congress's intent to promote fairness and efficiency in government disputes with private parties. Finally, notwithstanding Interior's attempt to characterize its claim for additional lease royalties as a statutory action seeking an equitable remedy, Interior's claim is plainly one founded on contract, seeking money damages.

## IV. ARGUMENT

### A. The D.C. Circuit's Decision Impermissibly Rewrites The Statute.

Section 2415(a) provides:

> (a) Subject to the provisions of section 2416 of this title, and except as otherwise provided by Congress, every action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later . . . .

The D.C. Circuit commenced its statutory analysis by observing that "[t]he threshold question is whether an administrative order assessing additional royalties can reasonably be understood to be an 'action for money damages' initiated by the filing of a 'complaint.'" Pet. App. at 16a. Reasoning that an "action for money damages" only includes "a suit in a court of law," the Court concluded that Interior can issue an "administrative compliance order" without regard to the six-year statute of limitations. *Id.* at 16a-17a. API respectfully urges the Court to reverse the D.C. Circuit's decision, under which Interior's ability to pursue additional royalty monies is subject to no time limit whatsoever.

API does not dispute that the requisite analysis must consider Congress's use of the term "complaint." Whether or not a complaint has been filed within six years after the United States' right of action accrues is plainly a critical question under the statute. As BP correctly argues in the Brief for Petitioner, numerous judicial, legislative, and administrative authorities support the conclusion that the term "complaint" as used in Section 2415(a) encompasses an administrative order, including an order issued by Interior to commence an action seeking payment of additional royalties. Moreover, as API has shown herein, a royalty payment order by Interior is certainly the functional equivalent of a judicial "complaint": such an order commences an adjudicative proceeding, it triggers a jurisdictional appeal period in which defenses must be formally asserted or be deemed waived, and its ultimate resolution lies in a suit for judicial review.

Because the Brief for Petitioner so thoroughly addresses the numerous authorities that support interpreting the term "complaint" to include an administrative royalty payment order, API will not repeat that argument in this amicus brief. However, API points out that it is not essential to characterize an Interior royalty payment order as a "complaint" to conclude that the six-year statute of limitations bars the royalty payment order at issue here. That is because Interior did *nothing* within the six-year period after Amoco Production Company made its original royalty payments. Having failed to take any action whatsoever, the result is clear: "*every* action . . . [is] barred," including Interior's administrative action seeking to collect additional royalties.

In its effort to avoid "strain[ing] legal language" by "construe[ing] this administrative compliance order as a

'complaint' for money damages," the D.C. Circuit twisted the clear language of the statute and committed the very error that it sought to avoid. Pet. App. at 17a. Tellingly, the D.C. Circuit's forced reading of the statute required it to constrict language – "every action" – that Congress clearly crafted to achieve an expansive reach. The D.C. Circuit's analysis is wrong because it effectively rewrites the statute so that "complaint" replaces the all-inclusive "every action." Under the D.C. Circuit's approach, the statute would read as follows:

> . . . except as otherwise provided by Congress, a complaint for money damages brought by the United States or an officer or agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues . . .

Neither Interior nor the courts are authorized to recast what Congress has written.

### B. Application Of Section 2415(a) To Interior Orders To Pay Royalties Respects Congress's Choice Of Language And Promotes A Consistent Interpretation Of All Subsections Of The Statute.

On its face, Section 2415(a) requires the following analysis when Interior issues a royalty payment order. If the Court agrees with BP that "complaint" includes such an administrative order, then Interior's order is barred if it is issued more than six years after the alleged royalty underpayment occurred. As noted above, however, even if the Court finds that the term "complaint" means a judicial filing, it still must be determined whether the United States

has filed a judicial complaint during the six-year period. If the United States has not filed a judicial complaint during that six-year period, then the statutory consequences are both sweeping and unavoidable: "*every action*" is barred, including Interior's administrative royalty collection action. In this case, which is typical of dozens of royalty disputes between API members and Interior, there is no question that Interior failed to file a judicial complaint, or take any action whatsoever, within the six-year period after the royalty payments were due. Having failed to file a complaint (whether administrative or judicial) within six years, the United States' action to recover additional royalties is time-barred.

An Interior order to pay royalties plainly commences an "action." The order places the lessee at risk of incurring penalties if the lessee fails either to pay or to protect itself by filing an appeal. The issuance of an order triggers a jurisdictional appeal period that subjects the lessee to the preclusive effects of waiver if the lessee fails to assert its defenses in a timely fashion. *Santa Fe Energy Co.*, 110 IBLA 209, 210 (1989). Interior itself has repeatedly recognized that its royalty payment orders are themselves "administrative actions." *E.g.*, *Marathon Oil Co.*, 149 IBLA 287, 291 (1999) (MMS demand for recalculation and payment of royalties "is not a judicial action for money damages brought by the United States, but is an administrative action not subject to the statute of limitations"); *Navajo Refining Co.*, 147 IBLA 253, 256 (1999) ("This is an administrative action initiated after completion of a contract reconciliation which found that the account had a balance due."); *W. A. Moncrief, Jr.*, 144 IBLA 13 (1998) (holding that demands for royalties and interest are "administrative actions"); *Anadarko Petroleum Corp.*, 122 IBLA 141, 147 (1992) (same).

Moreover, interpreting Section 2415(a) in the manner urged by API gives meaning to the entirety of Section 2415(a), as well as the remainder of Section 2415. For example, although Interior could file a judicial complaint to assert the United States' royalty claim, if Interior instead issues an administrative payment order within the six-year period, then the lessee's administrative appeal rights trigger the tolling of the six-year period for "applicable administrative proceedings required by contract or by law." 28 U.S.C. § 2415(a). In this provision of Section 2415(a), Congress expressly contemplated that an administrative appeal would toll the running of the limitations period. *See* S. Rep. No. 89-1328, at 2504 (1966). Obviously, for an administrative appeal to toll the limitations period, the order that is the subject of the administrative appeal must have been issued *within* the limitations period; otherwise there would be nothing left to toll. If Section 2415(a) does not apply to administrative orders to pay, this tolling provision would be meaningless. As this Court has long recognized, it is an "elementary canon" of statutory construction that a statute "should be interpreted so as not to render one part inoperative." *Dept. of Revenue of Or. v. ACF Indus., Inc.*, 510 U.S. 332, 340 (1994); *see also Colautti v. Franklin*, 439 U.S. 379, 392 (1979).

Similarly, including Interior's royalty payment orders within the scope of "actions" that are barred gives meaning to Section 2415(i), which provides:

> (i) The provisions of this section shall not prevent the United States or an officer or agency thereof from collecting any claim of the United States by means of administrative offset, in accordance with section 3716 of title 31.

If Section 2415(a) is construed not to apply to an administrative order to pay issued more than six years after the contractual

payment was due, there would have been no need for Section 2415(i) to exempt administrative offsets from the limitations period. Section 2415(i) was enacted precisely because Congress recognized that the statute has the meaning asserted by API – *i.e.*, that, absent an express exception, the statute of limitations prevents the government from pursuing alleged debts over six years old through any means. S. Rep. Nos. 97-378 & 97-287 (1982); *see also United States v. Hanover Ins. Co.*, 82 F.3d 1052, 1055 (Fed. Cir. 1996) ("Administrative offset is not a judicial action."). As with the tolling provision for "applicable administrative proceedings," the D.C. Circuit's statutory interpretation renders this section of the statute meaningless.

Finally, interpreting the six-year limitations period to apply to *every* action, administrative as well as judicial, not only gives meaning to all subsections of Section 2415, but such an interpretation is also compelled by the "'fundamental canon of statutory construction that the words of a statute must be read in their context and with a view to their place in the overall statutory scheme.'" *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 133 (2000) (quoting *Davis v. Michigan Dept. of Treasury*, 489 U.S. 803, 809 (1989)); *see also Pittsburgh & Lake Erie R.R. Co. v. Ry. Labor Executives' Ass'n*, 491 U.S. 490, 510 (1989) (noting the principle that two federal statutes should be read to make each effective). The overall statutory scheme for the royalty payments at issue here calls for "enforcement practices that ensure the prompt and proper collection" of royalties, 30 U.S.C. § 1701(b)(3), and imposes a six-year record keeping requirement on federal lessees. 30 U.S.C. § 1713(b). Given that Congress both directed Interior to act "promptly" and created a six-year period for a federal lessee to maintain accounting records after royalty payments were due, it defies logic to suggest that the six-year limitations period does not apply to a collection action that Interior commences by issuing a royalty payment order. *See Brown & Williamson*, 529 U.S. at

133 (noting that "the meaning of one statute may be affected by other Acts" and that the Court also must be guided by common sense).[3]

### C. Reading "Every Action" To Include "*Every* Action" Advances Congress's Purpose In Enacting The Statute Of Limitations.

The legislative history of Section 2415 further supports interpreting the statute to bar *all* untimely actions for money damages brought by the federal government, without carving out untimely actions initiated by administrative order. *E.g.*, S. Rep. No. 89-1328, at 2503-04 (1966) (noting that the statute was intended "to improve claims procedures" and that the statute of limitations would be applicable to "all Government actions based on contracts"); H.R. Rep. No. 89-1534, at 3-4 (1966) (same).[4]

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3. In 1996, Congress enacted the Federal Oil and Gas Royalty Simplification and Fairness Act, ("FOGRSFA"), which established a seven-year statute of limitations period for the government to assert royalty claims against federal lessees. 30 U.S.C. § 1724(b)(1). As the D.C. Circuit accurately observed, because FOGRSFA was made prospective only, the seven-year limitations period does not apply to the government's claim for additional royalties in this case. Pet. App. at 16a n.1. However, it is notable that, consistent with API's argument herein, in FOGRSFA Congress amended the record-keeping requirement to match the new seven-year limitations period for asserting royalty claims. *See* 30 U.S.C. § 1724(f) (requiring federal lessees to retain records for "the same period of time during which a judicial proceeding or demand may be commenced under subsection (b) this section.").

4. Certainly, the legislative history contains references to courts, litigants, and lawsuits. Yet, it also refers to the limitations period as being applicable to "monetary claims," "government claims for money," and simply "government claims." S. Rep. No. 89-1328, at 2503, 2513 (1966); H.R. Rep. No. 89-1534, at 3 (1966).

The legislative history makes clear that the central purpose of Section 2415 was to promote fairness by protecting private parties who contract with the federal government from exposure to stale claims and by making the federal government "more nearly equal to [the position] of private litigants." S. Rep. No. 89-1328, at 2513 (1966); H.R. Rep. No. 89-1534, at 10-11 (1966). Indeed, the Senate Report on the proposed statute explained:

> The *emphasis on fairness* . . . is a very important consideration and the *principal basis* for the bill.

S. Rep. No. 89-1328, at 2508 (1966) (emphasis added).

The concerns to which Section 2415 was addressed were further explained as follows:

> Many of the contract and tort claims asserted by the Government are almost indistinguishable from claims made by private individuals against the Government. Therefore it is only right that the law should provide a period of time within which the Government must bring suit on claims just as it now does as to claims of private individuals. The committee agrees that the equality of treatment in this regard provided by this bill is required by modern standards of fairness and equity.
>
> . . . The committee feels that the prompt resolution of the matters covered by the bill is necessary to an orderly and fair administration of justice. *Stale claims can neither be effectively presented or adjudicated in a manner which is fair to the parties involved.* Even if the passage of time does

> not prejudice the effective presentation of a claim, the mere preservation of records on the assumption that they will be required to substantiate a possible claim or an existing claim increases the cost of keeping records. As time passes the collection problems invariably increase. The Government has difficulty in even finding the individuals against whom it may have a claim for they may have died or simply disappeared. These problems have been brought to the attention of the committee previously in connection with other legislation. This bill provides the means to resolve these difficulties.

S. Rep. No. 89-1328, at 2503-04 (1966) (emphasis added); H.R. Rep. No. 89-1534, at 4 (1966) (emphasis added); *see also Phillips Petroleum Co. v. Lujan*, 4 F.3d 858, 863 (10th Cir. 1993) (stating that, in enacting Section 2415(a), "Congress was motivated in part by notions of fairness and equity in government dealings with private litigants, and further motivated to reduce the costs of record keeping and encourage prompt agency actions on claims"). The Senate and House Reports also noted that:

> enactment will reduce unnecessary litigation and court congestion, speed up meritorious settlements and cut down on unproductive paperwork. At the same time, the private litigants can be assured of a more fair and balanced treatment when dealing with the Government.

S. Rep. No. 89-1328, at 2503 (1966); H.R. Rep. No. 89-1534, at 3-4 (1966). The clearly expressed goal of assuring private litigants a "more fair and balanced treatment when dealing

with the Government," *id.*, provides compelling support for applying the six-year statute of limitations to all government collection claims, regardless whether such claims are commenced as administrative or judicial actions. *Cf.* 28 U.S.C. § 2401 (imposing six-year limitations period on contract claims by private parties against the government). This result is particularly called for when, as here, the government agency has the choice whether to commence its collection action in the judicial or administrative arena.

The problems associated with adjudicating old claims are especially pronounced in royalty collection matters. The complexities of royalty accounting, turnover of personnel with relevant factual knowledge, and changes in lease ownership and control of historical payment data combine to create tremendous difficulties for a lessee attempting to challenge the merits of an outdated royalty claim. These problems are exacerbated when Interior proceeds by issuing an administrative order to pay, because in the judicial review proceeding that inevitably follows, Interior uniformly asserts that it is entitled to judicial deference to its substantive royalty determination. The unfairness of this is obvious when the lessee's typical experience is considered: (1) first, the lessee makes its monthly royalty payment and Interior does nothing to challenge the accuracy of that payment for more than six years; (2) Interior then issues an administrative order to pay, and the lessee finds itself unable to develop the data necessary to challenge fully the merits of Interior's claim; (3) when the lessee files the administrative appeal that is essential to protect its defenses and avoid penalties, Interior's IBLA rejects the lessee's reliance on 28 U.S.C. § 2415(a) as being inapplicable to "underlying administrative actions" and renders a final agency decision upholding Interior's original order to pay; (4) when the lessee seeks judicial review,

Interior continues to assert that the statute of limitations does not apply, and Interior further asserts that the lessee must overcome the presumptive correctness of its substantive royalty determination, based on the rule of judicial deference to agency decisions; and (5) if Interior's claim is upheld on judicial review, the interest that the lessee owes often exceeds the principal amount of any alleged underpayment.

In view of the foregoing, it is actually to Interior's benefit to wait to issue its administrative order to pay until more than six years after the original royalty payment was owed: delay impairs the lessee's ability to defend the substance of Interior's claim, and it increases the government's ultimate monetary recovery. However, this sort of "coercive agency action[] predicated upon an otherwise time-barred claim," *United States v. Hanover Ins. Co.*, 82 F.3d 1052, 1055 (Fed. Cir. 1996), simply cannot be reconciled with Congress's clearly expressed concern for precluding stale claims and promoting fairness for private parties who contract with the government. Nothing in either the wording or the legislative history of the statute reasonably can be read to suggest that Congress authorized agencies to circumvent the limitations period through the "procedural gimmickry" of substituting administrative proceedings for government-initiated litigation. *OXY USA, Inc. v. Babbitt*, 268 F.3d 1001, 1006 (10th Cir. 2001). Interpreting "every action" to include "*every* action" – regardless whether commenced by an administrative order to pay or by a lawsuit – is the only interpretation that advances Congress's intent to promote "modern standards of fairness and equity." S. Rep. No. 89-1328, at 2503 (1966); H.R. Rep. No. 89-1534 at 4.

### D. Interior's Royalty Payment Orders Seek "Money Damages" And Are "Founded On Contract."

Contrary to Interior's protestations, Interior's administrative action to collect additional royalty payments clearly constitutes an "action for money damages," which is "founded upon a contract" for purposes of Section 2415.

Interior relies heavily on *Bowen v. Massachusetts*, 487 U.S. 879 (1988), in which the State of Massachusetts sued the United States for declaratory and injunctive relief from an order disallowing Medicaid reimbursement. Holding that the federal district court had jurisdiction, this Court concluded that the suit was not an action for "money damages" under the Administrative Procedure Act, 5 U.S.C. § 702. *Id.* at 893-900. In so holding, the Court opined that the phrase "relief other than money damages," as used to waive sovereign immunity under the Administrative Procedure Act, encompassed suits for the enforcement of statutory mandates, even though the mandate "happens to be one for the payment of money." *Id.* at 900. Grasping this language, Interior contends that its claim as a mineral lessor to recover additional lease royalties is a claim for equitable monetary relief rather than for "damages."

The holes in Interior's position are readily apparent. Neither the result nor the reasoning in *Bowen* can be stretched to reach the question before this Court because the posture of *Bowen* was so dramatically different from that of the present case. Unlike the action at issue in *Bowen*, Interior does not seek to enforce a statutory mandate in a dispute between two public bodies, but instead has initiated a lessor's royalty collection action against its lessee. *See OXY USA, Inc. v. Babbitt*, 268 F.3d 1001, 1008 (10th Cir. 2001)

(distinguishing *Bowen* and concluding that an MMS action to collect royalty payments is an action for money damages, founded upon a contract within the meaning of Section 2415). It is well recognized that federal oil and gas leases are contracts, under which the government's rights, as lessor, are generally governed by the law of contracts applicable to private parties. *E.g.*, *Mobil Oil Exploration & Prod. Southeast, Inc. v. United States*, 530 U.S. 604 (2000).

Further, that the federal leasing program is a creature of statute does not convert an Interior order to pay from an action "founded on contract" to an action founded on statutory mandate. As the Tenth Circuit correctly concluded:

> The fact that the Secretary of the Interior administers federal oil and gas leases through the MMS, applying applicable royalty assessment (valuation) and collection regulations promulgated in accordance with the Federal Oil and Gas Royalty Management Act, 30 U.S.C. § 1701 *et seq.*, and other mineral leasing statutes, simply does not change the contractual underpinnings of the lessee/lessor relationship or the legal source of the royalty payment obligation MMS seeks to enforce.

*OXY*, 268 F.3d at 1007. Under Interior's theory, *all* government claims for monies allegedly past due under a contract could be characterized as "equitable monetary relief," and Section 2415 would be inoperative as to the vast majority of government contract actions. Such a reading of the statute is patently untenable.

## V. CONCLUSION

For the reasons stated herein, the Court should reverse the D.C. Circuit decision.

Respectfully submitted,

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No. 05-669

IN THE

# Supreme Court of the United States

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BP America Production Company *et al.*,
*Petitioners*,

v.

Rejane Burton, Acting Assistant Secretary,
Land and Minerals Management,
Department of the Interior, *et al.*,
*Respondents*.

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**On Writ of Certiorari to the
United States Court of Appeals
for the District of Columbia Circuit**

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## BRIEF OF *AMICI CURIAE* JICARILLA APACHE NATION, SOUTHERN UTE INDIAN TRIBE, STATE OF NEW MEXICO, AND CALIFORNIA OFFICE OF THE STATE CONTROLLER IN SUPPORT OF RESPONDENTS

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No. 05-669

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**On Writ of Certiorari to the
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for the District of Columbia Circuit**

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## BRIEF OF *AMICI CURIAE* IN SUPPORT OF RESPONDENTS

The Jicarilla Apache Nation, Southern Ute Indian Tribe, State of New Mexico, and California Office of the State Controller respectfully submit this brief as *amici curiae* in support of Respondents.[1]

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[1] No counsel for any party authored any portion of this brief and no person or entity other than the *amicus curiae* made a monetary contribution to the preparation or submission of this brief. All parties to this case have consented to the filing of this brief, as indicated in letters filed with the Court.

## INTEREST OF *AMICI CURIAE*

"States and Indian landowners have an important stake in the full and correct payment of royalties." H.R. Rep. No. 97-859, at 15 (1982), *as reprinted in* 1982 U.S.C.C.A.N. 4269.

The States of California and New Mexico contain federal lands subject to thousands of oil and gas leases. Pursuant to the Mineral Leasing Act of 1920, 30 U.S.C. § 191(a) (2000), the states receive 50% of all royalties generated from these federal leases. This money supports a number of state programs, including schools, Medicaid, and water conservation projects.

The Jicarilla Apache Nation and the Southern Ute Indian Tribe are federally recognized Indian tribes located in northwest New Mexico and southwest Colorado, respectively. The tribes are the lessors and royalty owners of oil and gas leases issued under the Indian Mineral Leasing Act of 1938, 25 U.S.C. §§ 396a-396g (2000), and the Indian Mineral Development Act of 1982, 25 U.S.C. §§ 2101-2108 (2000). Royalties paid to the tribes from oil and gas production on these leases provide about half of all the revenue used to pay for essential government services on the tribes' reservations, such as police, tribal courts, health care, and education.

Lessees on Indian and federal lands initially pay royalties based on their own reports of the volume and value of their oil and gas production. *See* 30 C.F.R. part 210 (2005). These reports are subject to audit by the Minerals Management Service ("MMS"), the agency in the Department of the Interior ("Interior") responsible for managing federal and Indian oil and gas royalties. *See, e.g.*, 25 C.F.R. § 211.6; 30 C.F.R. part 210 (2005). In numerous instances, the MMS has issued orders to pay additional royalties to companies producing oil and gas

from the Jicarilla Apache and Southern Ute Reservations and from the *amici* States. Because of the complexity and retroactive nature of the audit process, many of these orders to pay involve periods that stretch back more than six years from the date of the orders. Application of the six-year statute of limitations in 28 U.S.C. § 2415(a) (2000) to these orders, as Petitioner BP America ("BP") urges, would render the amounts due to the tribes and states uncollectible. It also would result in a windfall to the oil and gas companies, who would in effect be rewarded for underreporting the amount of royalties they owed.[2]

## SUMMARY OF ARGUMENT

As the government has argued and *amici* agree, Congress spoke clearly in the Act of July 18, 1966, as amended, 28 U.S.C. § 2415(a), and provided a statute of limitations against the United States for judicial actions, not for administrative orders. Subsequent amendments to Section 2415(a) to preserve Indian contract claims confirm that Congress did not intend the six-year statute of limitations to apply to administrative orders. The statutory language, legislative history, and administrative actions regarding Indian contract claims all demonstrate that Section 2415(a) applies only to "litigation" and "suits" brought by the United States in "court."

Congress confirmed this interpretation of the statute as regards royalty management when it enacted subsequent legislation in that specific field. The text and legislative history

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[2] Atlantic Richfield Company, the second petitioner in this case, did not raise the statute of limitations below and in any event is wholly owned by BP. Pet. Br. at iii. This brief therefore references only "BP" or "Petitioner" in the singular.

of the Federal Oil and Gas Royalty Management Act of 1982 ("FOGRMA"), Pub. L. No. 97-451, 96 Stat. 2447 (1983), codified at 30 U.S.C. §§ 1701-1757 (2000), and the amendments to FOGRMA in the Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 ("RSFA"), Pub. L. No. 104-185, 110 Stat. 1700 (1996), demonstrate that Congress did not intend Section 2415(a) to apply to MMS orders for royalty payment.

Congress enacted FOGRMA in 1983 in order to address a problem dating back to the 1960's involving massive underpayments of federal and Indian oil and gas royalties. To remedy the problem, Congress prescribed more comprehensive audits by MMS of industry reports and payments of royalties, a goal that does not at all support an intent to limit the time for conducting those administrative audits.

In RSFA, enacted another 14 years later, Congress imposed a seven-year statute of limitations against the United States for royalty collections and explicitly applied the limit to both judicial and administrative actions. 30 U.S.C. § 1724. The statutory language and legislative history show that Congress intended to impose a *new* statute of limitations for such administrative actions, not an amendment or revision to Section 2415(a). Congress' intent is particularly evident in its express exemption of Indian lands from this new seven-year statute of limitations. 30 U.S.C. § 1701 note. If Section 2415(a) applied to MMS orders, the Indian exemption in the new law would make administrative orders enforcing tribal oil and gas royalties subject to the *shorter* six-year statute in Section 2415(a), a consequence clearly not contemplated by Congress, especially in light of the federal government's trust responsibility toward tribes.

The fact that Section 2415(a) does not apply to administrative orders for payment of royalties imposes no unfair burdens on oil and gas lessees. The original bargain struck through BP's leases included no statute of limitations on government claims for underpayment of royalties, neither judicial nor administrative. Furthermore, the history of malfeasance in the payment of royalties under federal and Indian oil and gas leases and the resulting Congressional actions strengthening royalty oversight and enforcement through FOGRMA make clear that Congress did not intend a period of repose for orders to pay oil and gas royalties until it passed RSFA in 1996.

Thus, the plain statutory language of Section 2415(a), its subsequent amendments preserving claims regarding Indians, and the language and legislative history of FOGRMA and RSFA all serve to support affirmance of the D.C. Circuit's opinion in this case. To hold otherwise would undermine the role of MMS in enforcing royalty obligations, causing unnecessary litigation and unjustly harming the states and tribes who have relied on MMS oversight.

## ARGUMENT

### I. The Amendments to Section 2415(a) Extending the Statute of Limitations for Indian Contract Claims Confirm that Section 2415(a) Applies to Judicial, Not Administrative, Actions.

The plain language of Section 2415(a) establishes a six-year statute of limitations for *judicial* actions brought by the United States. Section 2415(a) provides as follows:

> every *action for money damages* brought by the United States . . . which is founded upon any contract . . . shall be barred unless the *complaint* is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable *administrative proceedings* . . . , whichever is later.

(Emphasis added.) Congress used terms in this provision specifically associated with judicial actions, such as "action for money damages," which the D.C. Circuit below noted "points strongly to a suit in a court of law, rather than an agency enforcement order that happens to concern money due under a statutory scheme." *Amoco Production Co. v. Watson*, 410 F.3d 722, 733 (2005) (Pet. App. 16a). Moreover, Section 2415(a) ties the running of the statute of limitations to the filing of a "complaint" and refers to the time when the "right of action accrues," also terms associated with judicial claims. Congress then contrasted this judicial action with *administrative* activity, providing that an "action for money damages" may be brought within one year of a final decision in an administrative proceeding. Congress thus was not creating a statute of limitations for administrative orders, but was concerned about the time for bringing an action in the federal courts.

*Amici* concur with all of the United States' arguments on these issues – on the express language of the statute, as well as on the rules of statutory construction and the legislative history of Section 2415 – and do not repeat them here to avoid duplication. Instead, *amici* explain how the amendments to Section 2415(a) extending the statute of limitations for Indian contract claims confirm that the statute applies only to judicial, not administrative, claims.

Congress amended Section 2415(a) on several occasions, beginning in 1972 and continuing through 1982, to

extend the time for the United States to bring Indian contract claims, as reflected in the provisos following the main portion of Section 2415(a).[3] BP argues that these provisos somehow demonstrate that Section 2415(a) applies to administrative orders. On the contrary, both the language and the legislative history of the Indian claims amendments confirm that Section 2415(a) applies to judicial actions only.[4]

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[3] *See* An Act to extend for ninety days the time for commencing actions on behalf of an Indian tribe band, or group, Pub. L. No. 92-353, 86 Stat. 499 (1972); An Act to extend the time for commencing actions on behalf of an Indian tribe, band, or group, Pub. L. No. 92-485, 86 Stat. 803 (1972); An Act to amend the statute of limitations provisions in section 2415 of title 28, United States Code, relating to claims by the United States on behalf of Indians, Pub. L. No. 95-64, 91 Stat. 268 (1977); An Act to amend the statute of limitations provisions in section 2415 of title 28, United States Code, relating to the claims by the United States on behalf of Indians, Pub. L. No. 95-103, 91 Stat. 842 (1977); An Act to extend the time for commencing actions on behalf of an Indian tribe, band, or group, or on behalf of an individual Indian whose land is held in trust or restricted status, Pub. L. No. 96-217, 94 Stat. 126 (1980); Indian Claims Limitation Act of 1982, Pub. L. No. 97-364, 96 Stat. 1966 (1982).

[4] The full text of the relevant provisos in Section 2415(a) reads as follows:

> *Provided further,* That an action for money damages brought by the United States for or on behalf of a recognized tribe, band or group of American Indians shall not be barred unless the complaint is filed more than six years and ninety days after the right of action accrued: *Provided further,* That an action for money damages which accrued on the date of enactment of this Act in accordance with subsection (g) brought by the United States for or on behalf of a recognized tribe, band, or group of American Indians, or on behalf of an individual Indian whose land is held in trust or restricted status, shall not be barred unless the complaint is filed sixty days after the date of publication of the list required by Section 4(c) of the Indian Claims Limitation Act of 1982: *Provided*, That, for those claims that are on either of the two lists

(continued...)

First, the language describing the types of actions to which the provisos apply is the same in all relevant particulars as the language in the main part of Section 2415(a), which, as discussed above and argued by the United States, pertains only to judicial actions. The first proviso added by the amendments (allowing an additional 90 days for the United States to bring Indian contract claims) specifies that the statute of limitations applies to an "action for money damages" for which a "complaint" is filed, just as in the main part of subsection (a). The second proviso (which, together with subsection (g), extends the time on which Indian contract claims accrue) also contains this language. Finally, the third proviso contains both this language and also the same distinction as in the main portion of subsection (a) between a "right of action" enforced by a "complaint" and a "final decision . . . rendered in applicable administrative proceedings."

The legislative history of the Indian contract claims amendments supports the plain reading of the amendments and of the identical language in the main body of Section 2415(a) as applying to judicial actions only. The Indian contract claims legislation was enacted because the Department of the Interior was aware that Section 2415(a) imposed a statute of

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[4](...continued)
published pursuant to the Indian Claims Limitation Act of 1982, any right of action shall be barred unless the complaint is filed within (1) one year after the Secretary of the Interior has published in the Federal Register a notice rejecting such claim or (2) three years after the date the Secretary of the Interior has submitted legislation or legislative report to Congress to resolve such claim or more than two years after a final decision has been rendered in applicable administrative proceedings required by contract or by law, whichever is later.

limitations on "contract *suits* brought by the United States;" Interior stated that it required more time "to identify all of these wrongs and then develop factual information necessary to get *litigation filed*" and that "[t]his inability to *prosecute* the present claims of Indians will work a hardship on tribes." S. Rep. No. 92-1253, at 2-4 (1972); H.R. Rep. No. 92-1267, at 3 (1972) (emphasis added). The reports also refer to "*prosecuting* the claims in the *courts*." S. Rep. No. 92-1253 at 3; H.R. Rep. No. 92-1267 at 4 (emphasis added); *see also* S. Rep. No. 92-1253 at 4, H.R. Rep. No. 92-1267 at 3-7 (other instances referring to "prosecuting" a claim). The legislative history of subsequent amendments is similar. *See, e.g.*, H.R. Rep. No. 95-375, at 3, 7 (1977), *as reprinted in* 1977 U.S.C.C.A.N. 1616 (recognizing that Interior must identify and investigate claims before it can refer them to the "Justice Department for *litigation*" and supporting extending the statute of limitations for "*suits* brought by the Government on behalf of Indians" to "afford the Government additional time to . . . prepare for *litigation*") (emphasis added); *accord* H.R. Rep. No. 96-807, at 8, 10 (1980) (supporting the extension "for filing certain *lawsuits* on behalf of Indian individuals or tribes to recover monetary damages" and to address certain "particulars without which *suit* cannot be filed") (emphasis added). The legislative history thus makes clear that the amendments addressed a statute of limitations for judicial actions.

The hearing testimony that Petitioner cites does not warrant any different interpretation. *See Time Extension for Commencing Actions on Behalf of Indians: Hearing on S. 3377 and H.R. 13825 Before the Subcommittee on Indian Affairs of the Committee on Interior and Insular Affairs*, 92d Cong., 2d Sess. (1972) (joint statement of Arthur Lazarus, Jr., Marvin Sonosky, and Charles A. Hobbs, Attorneys' Panel). The reference to "violations of lease agreements" in the testimony

does not necessitate a conclusion that the actions subject to Section 2415(a) include administrative royalty orders; in fact, the testimony specifically states that the claims discussed "are claims that would be filed in the Federal district court." *Id.* at 31; *see also id.* at 37-38 (referring to "suits" throughout, as well as to "litigants").[5]

Finally, Petitioner's reliance on the Federal Register lists published pursuant to the Indian Claims Limitation Act ("ICLA"), Pub. L. No. 97-394, 96 Stat. 1966 (1982), is also misplaced, because these lists also deal with judicial, not administrative, claims. The ICLA, referenced in the second and third provisos added to Section 2415(a), required the Secretary of the Interior to publish a list of all Indian claims identified under the "Statute of Limitations Project" and accruing on or before July 18, 1966, the effective date of Section 2415. ICLA § 3(a). The referenced "Statute of Limitations Project" was established by the 1980 amendments to Section 2415, Pub. L. No. 96-217, and required the Secretary to identify claims appropriate either for *litigation* or legislation.[6] Individual Indians, Indian tribes and other Indian groups then had six months to propose additional claims to be

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[5] The testimony included the following exchange:

> MR. LAZARUS: These are claims that would be filed in Federal district court.
> SENATOR FANNIN: I think that was made plain.

*Id.* at 31.

[6] Pub. L. No. 96-217, § 1 required the Secretary to commence actions for money damages for pre-1966 Indian claims by filing complaints by December 31, 1982 and, in § 2, required the Secretary to submit legislative proposals to Congress to "resolve those Indian claims subject to . . . the first section of this Act that . . . are not appropriate to resolve by *litigation*" (emphasis added).

considered "for *litigation* or legislation by the United States," and the Secretary was to include these claims on a revised list. ICLA §§ 4(a), 4(c) (emphasis added). The Secretary could "reject for *litigation* any of the claims" contained on the two lists and could submit the claim instead for legislation pursuant to Section 6(a). ICLA § 5(b) (emphasis added). Rejected claims were to be listed in a third Federal Register notice, and "potential individual Indian *plaintiffs*" were required to file a "*complaint*" on such claims within one year of publication. ICLA §§ 5(b), 5(c) (emphasis added). This Congressional language makes clear that the two Federal Register lists cited by Petitioner do not pertain to administrative claims. *See* 48 Fed. Reg. 13,698 (Mar. 31, 1983); 48 Fed. Reg. 51,204 (Nov. 7, 1983).[7]

The text and background of the Indian contract claims amendments therefore support the D.C. Circuit's opinion that Section 2415(a) limits only judicial actions, not administrative orders. Subsequent legislation pertaining to oil and gas royalty collection provides even further support.

## II. Congress Demonstrated Through FOGRMA and RSFA that Section 2415(a) Does Not Apply to MMS Orders to Pay Royalties.

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[7] Nor do the third and other subsequent lists published by Interior in the Federal Register pertain to administrative claims. Those lists each refer to the relevant time limit for filing a "complaint" on "any right of action on any claim appearing on the following list of claims" as the date "to file an *action in court*," and require submission of the "names of potential *plaintiffs* and *defendants*." *See* 54 Fed. Reg. 52,071 (Dec. 20, 1989); 55 Fed. Reg. 50,660 (Dec. 7, 1990); 56 Fed. Reg. 66,304 (Dec. 20, 1991); 57 Fed. Reg. 62,112 (Dec. 29, 1992) (corrected by 58 Fed. Reg. 17,042 (Mar. 31, 1993)); 59 Fed. Reg. 3,970 (Jan. 27, 1994) (emphasis added).

### A. The Legislative History of FOGRMA Confirms that Congress Did Not Contemplate a Six-Year Statute of Limitations for Administrative Orders to Pay Royalties.

As a sovereign, the United States is subject only to the statutes of limitations that it imposes on itself by Act of Congress. *See Metropolitan R. Co. v. District of Columbia*, 132 U.S. 1, *11 (1889); *United States v. Trio-No Enterprises, Inc.*, 819 F.2d 154, 158 (7th Cir. 1987); *United States v. City of Palm Beach Gardens*, 635 F.2d 337, 339 (5th Cir.), *cert. denied* 454 U.S. 1081 (1981); Pet. Br. at 3. While the 1966 Act imposed a general statute of limitations against the federal government on "actions for money damages" founded on contract, the question at issue here is whether this general limitation applies to the specific administrative orders for royalty payments issued by MMS in this case. This Court has often stated that a determination of the "meaning of one statute may be affected by other Acts, particularly where Congress has spoken subsequently and more specifically to the topic at hand." *F.D.A. v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 133 (2000) (citing *United States v. Estate of Romani*, 523 U.S. 517, 530-31 (1998)); *United States v. Fausto*, 484 U.S. 439, 453 (1988); *see also Scheidler v. N.O.W.*, ___ U.S. ___, 126 S. Ct. 1264, 1273 (2006) (a later, more specific statute aimed directly at the type of activity at issue suggested that the more general Hobbs Act did not apply). When Congress passed FOGRMA, it was clear that Congress did not view the six-year statute of limitations in Section 2415(a) as applying to the administrative collection of oil and gas royalties.

Congress enacted FOGRMA in 1983 in the wake of scandals involving massive underpayments of federal and Indian oil and gas royalties; as a consequence, FOGRMA was

intended to provide a more rigorous enforcement and oversight regime for royalty collection. *See* Section III.B, below; 30 U.S.C. § 1701. There is therefore no indication in the original FOGRMA of any intent to protect the oil and gas industry from administrative orders issued to collect underpaid royalties. When the Act was passed, the only statute of limitations in FOGRMA pertained to actions to recover *penalties*. *See* 30 U.S.C. § 1755.[8]

When deliberating the original FOGRMA legislation, moreover, Congress clearly did not act as if the six-year statute of limitations in Section 2415 applied to MMS orders such as the ones in this case. Discussing the record-keeping provisions in Section 103 of the statute (codified as 30 U.S.C. § 1713), the House Committee on Interior and Insular Affairs stated that "[t]he Committee intends that the Secretary will require that records be maintained beyond the 6-year [record retention] limit only for such period that he is diligently pursuing an audit." H.R. Rep. No. 97-859, at 18. An MMS order for payment of additional royalties follows an audit, as do any administrative appeals by the company or any other enforcement actions by the agency. *See, e.g.*, 30 C.F.R. parts 217, 218, 290 (2005). Thus, the Committee obviously

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[8] BP argues that a statute of limitations is important because MMS imposes interest on late payments, pursuant to 30 U.S.C. § 1721(a). That interest is not punitive, however, but simply accounts for the time value of money. The companies have had the use of the money during the entire period that royalties have gone unpaid. *Sanguine Ltd*, 155 IBLA 277, 283 (2001) ("late payment charges are not a penalty; they merely compensate the lessor for the time value of money owing but not timely paid, the use of which the lessee enjoys during the period the amount is unpaid"); *Stream Energy, Inc.*, 146 IBLA 130, 133 (1998); *Shell Offshore, Inc.*, 115 IBLA 205, 212 (1990); *Coastal Oil & Gas Corp.*, 108 IBLA 62, 67 (1989).

contemplated agency action to collect unpaid royalties well beyond six years.[9]

### B. The Addition of an Express Seven-Year Statute of Limitations in RSFA for MMS Orders to Pay Royalties Supports the Interpretation that the General Six-Year Statute of Limitations in Section 2415(a) Does Not Apply to Them.

Fourteen years later, Congress demonstrated that if it wants to set a statute of limitations for MMS administrative orders, it knows how to do so. In 1996, Congress passed RSFA, an amendment to FOGRMA and the only legislation to specifically address the statute of limitations for administrative actions to collect royalties. RSFA provided a seven-year statute of limitations for the United States to seek additional royalties from oil and gas producers, RSFA § 4, 30 U.S.C. § 1724, and applied this deadline both to judicial claims and to "demands," which it defined to include MMS orders to pay royalties,

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[9] BP's complaint about onerous record-keeping is exaggerated. Under MMS regulations, the company must file reports of mineral production, price of minerals sold, and amount of royalty payments made, all of which are kept by MMS indefinitely and are available to the company. *See* 30 C.F.R. §§ 210.10, 210.50-.55, 216.50-.55 (describing required forms); 216.25 (availability) (2005). Moreover, the company is made aware if MMS is reviewing records as part of an audit, *see* 30 C.F.R. §§ 212.50-.51, and MMS allows the company time to produce records for inspection, *see, e.g.*, 30 C.F.R. § 212.51(c). The legislative history of FOGRMA confirms that Congress did not envision record-keeping as an onerous burden: "The committee intends that the Secretary will require that records be maintained beyond the 6-year limit only for such period that he is diligently pursuing an audit and will release the record holder of his obligation to maintain records at the earliest possible date." H.R. Rep. No. 97-859, at 29; *accord* 30 C.F.R. §§ 212.50-.51.

30 U.S.C. § 1702(23). Congress also made clear that this statute of limitations does not apply to MMS collection of royalties for Indian tribes. RSFA § 9, 30 U.S.C. § 1701 note ("The amendments made by this Act shall not apply with respect to Indian lands, and the provisions of [FOGRMA]. . . as in effect on the day before the date of enactment of this Act [Aug. 13, 1996] shall continue to apply after such date with respect to Indian lands.").[10]

The fact that Congress added to FOGRMA an express statute of limitations on royalty collection and made it clear that the statute applied to administrative orders, or "demands," as well as to judicial claims indicates that Congress in 1996 did not understand the general statute of limitations in Section 2415(a) to apply to MMS administrative orders under FOGRMA. Moreover, the fact that the RSFA statute of limitations is seven years rather than six indicates that Congress was not seeking to clarify Section 2415(a) but was creating an

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[10] RSFA also does not apply to other minerals, such as coal, or to geothermal resources. *See* RSFA §§ 2,4, 30 U.S.C. §§ 1702(25) and (28), 1712, 1724. Thus, although administrative orders to collect oil and gas royalties from federal lands are subject to the seven-year statute of limitations for oil and gas produced after August 1996, such orders regarding royalties for coal on federal lands, which bring in millions of dollars a year to the federal and state governments, are not. *See* 30 U.S.C. §§ 191, 207 (states receive 50% of revenues from "rentals of the public lands," including coal leases, within state boundaries); Minerals Revenue Management, Minerals Management Service, U.S. Dept. of Interior, Reported Royalty Revenue by Category (reporting revenues from American Indian coal royalties for 2003-2005 ranging from approximately $55 million to $100 million, and total revenues from coal royalties for 2003-2005 ranging from approximately $460 million to $540 million). *See* http://www.mrm.mms.gov/MRMWebStats (last visited July 31, 2006) (providing links to information regarding royalty revenues for gas, coal, oil, and other royalties from 2001 forward).

entirely *new* statute of limitations on administrative orders for royalty collection.

The RSFA legislative history lends support to this interpretation. The House Report on RSFA states that this "new Section 115 to FOGRMA" was "add[ed] to *establish* limitation periods," not to amend or alter them. H.R. Rep. No. 104-667, at 18 (1996) (emphasis added); *accord* 142 Cong. Rec. S9675-05, at S9676 (1996) (Senator Murkowski's introduction of the RSFA bill); *id.* at S9676 (Letter from Secretary of the Interior to Sen. Murkowski (Jun. 6, 1996)); 142 Cong. Rec. S8369-02 (1996) (introduction of the bill by Sen. Bingaman for final passage). The minority statement in the House report confirms that Congress did not believe that any prior statute of limitations applied to MMS orders. In lamenting the enactment of the new seven-year statute of limitations in RSFA, the minority states that "*[h]ad the statute of limitations been in effect*, [Interior] would have been unable [in 1996] to investigate" an alleged conspiracy in California "during the period of 1978 to 1993" that was then under investigation. H.R. Rep. No. 104-667 at 49 (emphasis added).

Moreover, since RSFA does not apply to Indian lands, applying Section 2415(a) to administrative orders would have the result, after September 1, 1996, of Section 2415(a) applying *only* to oil and gas produced from Indian lands and not to oil and gas produced from federal lands, which are subject to the RSFA statute of limitations. *See* 30 U.S.C. § 1724.[11] In other words, royalty orders for Indian lands would be subject to a six-year statute of limitations, whereas royalty orders for federal lands would be subject to a seven-year statute of limitations.

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[11] The seven-year statute of limitations in RSFA became effective on September 1, 1996, the "first day of the month following August 13, 1996." 30 U.S.C. § 1724 note; RSFA § 11, 30 U.S.C. § 1701 note.

Considering the long-standing federal trust responsibility to Indian tribes, it would not merely be a peculiar result for a *shorter* limitations period to apply to Indian lands, but it would in fact be antithetical to that trust relationship, since it would undercut the United States' heightened duty to enforce Indian leases. *See generally Seminole Nation v. United States*, 316 U.S. 286, 296-97 (1942) (United States has a "moral obligation[] of the highest responsibility and trust" to Indian tribes and the federal government's "conduct . . . in dealings with the Indians, should therefore be judged by the most exacting fiduciary standards."); *Jicarilla Apache Tribe v. Supron Energy Corp.*, 728 F.2d 1555, 1563 (10th Cir. 1984) (Seymour, J., dissenting), *dissenting opinion adopted by court en banc*, 782 F.2d 855 (10th Cir. 1986), *modified*, 793 F. 2d 1171 (10th Cir. 1986), *cert. denied,* 479 U.S. 970 (1986) (holding that the Secretary is obligated to act as a fiduciary in the administration of tribal oil and gas reserves and therefore her "actions must not merely meet the minimal requirements of administrative law, but must also pass scrutiny under the more stringent standards demanded of a fiduciary"); *Pawnee v. United States,* 830 F.2d 187, 190 (Fed. Cir. 1987), *cert. denied*, 486 U.S. 1032 (1988) ("United States has a general fiduciary obligation toward the Indians with respect to the management of . . . oil and gas leases"); 30 U.S.C. § 1701 (referring to the Secretary's "trust responsibility in the administration of Indian oil and gas"); 30 C.F.R. § 206.170(e) (2005) (referring to "the trust responsibilities of the United States with respect to the administration of Indian oil and gas leases").

Congressional testimony regarding RSFA provides further evidence that, at the time of passage of RSFA, the parties understood that the Indian lands exemption would keep tribal lands from being burdened by a statute of limitations at all, and certainly would not subject tribal lands to a *shorter* limitations period than RSFA provides. In her testimony on the

proposed RSFA statute, the MMS Director – the head of the very agency tasked with royalty collection and enforcement – stated that the MMS "welcome[d] the fact that this bill would not apply to Indian leases, but . . . question[ed] why the Federal Government's obligation to the taxpayer for its oil and gas resources should be substantially *less than* it is to the Indian community for its oil and gas resources." *Clarification of Royalty Procedures: Before the House Subcommittee on Energy and Minerals Resources,* 1995 WL 435736 (July 18, 1995) (testimony of Cynthia Quarterman, Director, Minerals Management Service, Department of the Interior) (emphasis added). While the MMS Director's statement too readily dismisses the heightened federal trust responsibility toward tribes, it plainly evidences the general understanding at the time of RSFA's passage that exempting tribal lands from the statute would provide tribes with *additional* protections.

## III. There is No Inherent Unfairness in the D.C. Circuit's Ruling.

### A. When BP/Amoco Entered into the Leases at Issue there was No Statute of Limitations Against the United States, Neither Administrative Nor Judicial.

Amoco Production Company ("Amoco"), BP's predecessor in interest, "entered into leases with the Secretary of the Interior" approximately "a half-century ago." Pet. Br. at 7. At that time, according to BP's own brief in this case, "there was no general statute of limitations governing actions *by the United States* against private parties for breach of [contract]." *Id.* (emphasis in original). Such suits "ordinarily were governed by the rule *quod nullum tempus occurit regi* – 'no time shall run against the King' – and the United States had an

infinite amount of time within which to seek recovery." *Id.* This was the state of the law and thus part of the bargain Amoco knowingly struck when it entered into the leases which are now the subject of this case. Without expecting repose of any sort for liability for potential royalty miscalculations, intentional or otherwise, Amoco entered into a consensual lease relationship with the United States to extract and reap the financial benefits of 7/8 of the oil and gas production on tracts leased in the San Juan Basin.[12]

It is for Congress to determine when and whether a limitations period in the context of oil and gas royalty enforcement is in the national interest. The plainest, most straightforward reading of Section 2415 and the express statute of limitations in RSFA show that Congress simply did not act in the area of MMS orders to pay royalties until 1996, at which point Congress specifically provided a seven-year limitation on the United States for such administrative orders, expressly excluding solid minerals and Indian lands.

The fact that Congress waited until 1996 to provide a statute of limitations on MMS orders to pay royalties does not create anomalies in the law that this Court must fill through judicial construction. On the contrary, it is commonplace for Congress to choose to legislate on *some* matters in a particular field without addressing *all* matters in that field. *See, e.g.,*

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[12] Oil and gas companies enter into standard leases on federal and Indian lands in which they historically have received a right to 7/8 or 5/6 of the production. Thus, the lessees' obligation is to pay a royalty of only 1/8 or 1/6, based on the "fair market value" of the production. The leases also provide that the fair market value is subject to regulations in effect or to be put in effect by the government. Under Amoco's (now BP's) leases, the company obtained the right to 7/8 of the value of the mineral production. Pet. Br. at 7.

*Snapp v. Unlimited Concepts, Inc.*, 208 F.3d 928 (11th Cir. 2000):

> [W]e should not be quick to conclude that Congress either neglected to consider an issue related to its enactments, or decided to avoid the issue and leave its resolution to the courts. Such a predisposition on our part makes for activist judges and lazy Congressmen. Instead, we should search the statutory language and structure *with the assumption that Congress knew what it was doing* when it enacted the statute at issue.

*Id.* at 936 (emphasis added); *see also United States v. Azeem*, 946 F.2d 13, 17 (2d Cir. 1991) ("not every congressional silence is pregnant"); *Ohio Nat'l Bank v. Berlin*, 26 App. D.C. 218, 1905 WL 17656, at *3 (C.A.D.C. 1905) (it is not for the court to read legislation to embrace some cases only because a party argues that there is no good reason why those cases were excluded); *United States v. Union Pacific R. Co.*, 91 U.S. 72, 86 (1875) (the court "cannot supply omissions in legislation nor afford relief because [omissions] are supposed to exist."). There is nothing inherently unfair about Congress acting to provide limited repose to an existing consensual relationship in 1996 rather than 1966, particularly when one considers the history of royalty underpayment by oil and gas companies.

### B. The 50-Year History of Industry Underpayment of Federal and Indian Oil and Gas Royalties Demonstrates that Congress Intended No Broad Repose from MMS Orders to Pay Royalties until 1996.

BP makes much of the general purpose of repose underlying statutes of limitations, and attempts to apply that

principle to explain what Congress *should have done* in crafting Section 2415(a). However, "vague notions of a statute's 'basic purpose' are . . . inadequate to overcome the words of its text regarding the specific issue under consideration." *Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 220 (2002) (quoting *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 261 (1993)). The general societal benefit of establishing a period of repose in certain circumstances cannot trump the wording of Section 2415(a) or be allowed to undermine the important societal benefit that Congress intended by demanding proper enforcement and collection of royalties.

A statute cannot be "divorced from the circumstances existing at the time it was passed." *United States v. Champlin Refining Co.*, 341 U.S. 290, 297 (1951). During the 1960's and 1970's – including the very time that Congress was debating the passage of Section 2415 – the oil and gas industry was embroiled in a national scandal involving the theft of federal and Indian mineral resources by third parties and the underreporting of federal and Indian oil and gas royalties by hundreds of millions of dollars each year. In 1981, in response to these disturbing allegations, James Watt, the Secretary of the Interior during the Reagan administration, created a commission to investigate whether oil and gas companies were failing to report and pay royalty revenues properly: the so-called Linowes Commission. *See generally* Report of the Commission, Fiscal Accountability of the Nation's Energy Resources (Jan. 1982) ("Linowes Commission Report") (selected portions at Amicus App. 1a-7a).

The Linowes Commission was established to investigate "serious allegations of massive irregularities in royalty payments due the Federal government, Indian tribes, and States." *Id.* at 1a. The Linowes Commission determined that there were in fact "massive irregularities" in the calculation

of royalty revenues, costing States, Indian tribes, and U.S. taxpayers "hundreds of millions of dollars" in unpaid royalties:

> Management of royalties for the Nation's energy resources has been a failure for more than 20 years. Because the Federal government has not adequately managed this multibillion dollar enterprise, the oil and gas industry is not paying all the royalties it rightly owes . . . . The results of individual audits, which have often uncovered large underpayments, suggest that hundreds of millions of dollars due the U.S. Treasury, the States, and Indian tribes are going uncollected every year.

*Id.* at 3a. The Commission concluded that "undervaluation of natural gas was the largest factor in royalty underpayments," and that this problem was due in large part to the fact that the federal government "routinely accepts oil and gas companies' valuation of the product on which royalties are paid." *Id.* at 4a; *see also id.* at 7a (detailing one example of a company that underpaid more than $2 million from 1966 to 1976).

Decades of industry underpayments of hundreds of millions of dollars in federal and Indian royalties led Congress to enact FOGRMA, to "reaffirm, clarify and expand" the Secretary's authority to determine and collect the full amount of oil and gas royalties due under Federal and Indian leases. 30 U.S.C. § 1701(b)(1). FOGRMA's drafters explained that "States and Indian landowners have an important stake in the full and correct payment of royalties." H. Rep. No. 97-859, at 15. In particular, FOGRMA declares that "the Secretary should aggressively carry out his trust responsibility in the administration of Indian oil and gas." 30 U.S.C. § 1701(a)(4).

BP and supporting *amici* portray the oil and gas industry as the victim of a capricious federal bureaucracy. But the industry is not a victim, and it is not the federal government at fault here but the oil companies themselves.[13] Too often, states, tribes, and taxpayers have been denied their rightful royalty payments through oil and gas industry accounting schemes designed to reduce payments and inflate cost "allowances." *See United States v. Chevron U.S.A., Inc.*, 186 F.3d 644 (5th Cir. 1999); *United States ex rel. Koch v. Koch Indus., Inc.*, 57 F. Supp. 2d 1122 (N.D. Okla. 1999) (detailing numerous federal investigations and lawsuits seeking to disgorge improper oil company profits made through schemes to undervalue oil and gas production); *accord United States ex rel. Johnson v. Shell Oil Co.*, 33 F. Supp. 2d 528, 534-40 (E.D. Tex. 1999).

Other False Claims Act lawsuits filed by industry whistle-blowers are still pending in the courts, providing evidence that some in the oil and gas industry continue intentionally to underreport royalties. These lawsuits explain how lessees undervalue gas using a variety of schemes, including by calculating royalties based on sales to affiliates instead of arm's-length transactions; deducting more than the actual costs incurred for transportation and processing services; and undermeasuring and undervaluing gas and natural gas liquids. *See, e.g., United States ex rel Harrold E. (Gene) Wright v. AGIP Petroleum Co.*, No. 9:98CV30 (E.D. Tex. filed February 3, 1998), transferred No. 5:03-CV-264 (E.D. Tex.); *In*

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[13] BP continues to argue that it acted in compliance with the existing law regarding royalty calculation, even after the D.C. Circuit found otherwise and this Court denied certiorari on that point. *See* Pet. Br. at 7 ("Consistent with 60 years of Department of Interior and [MMS] practice, Amoco calculated the royalty as a percentage of the value of production . . . from the lease by determining the value of the gas as produced at the wells") (internal quotations omitted). The law of the case is directly to the contrary of BP's assertion. 410 F.3d at 727-730.

*re Natural Gas Royalties Qui Tam Litigation*, No. 1:99-md-01293-WFD (D. Wyo. filed Oct. 22, 1999) (consolidating 66 actions in eight districts). MMS has also specifically identified such unlawful practices. *See, e.g., Union Texas Petroleum*, 153 IBLA 170, 172 (2000) (failure to perform dual accounting;[14] failure to use accurate volumes and Btu measurements; undervaluation of gas by using contract price instead of maximum lawful price; taking processing allowance greater than actual cost); *Marathon Oil Co.*, 149 IBLA 287, 292-93 (1999) (failure to dual account); *ARCO*, 131 IBLA 299, 304 (1994) (undervaluation of production due to mis-categorization of oil); *Amoco Production Co.*, 123 IBLA 278, 293 (1992) (repeated royalty underpayments caused by erroneous claims for refunds).

Given this indisputable history, the general principle of repose underlying statutes of limitations, as invoked by BP, is merely a "vague notion[] of a statute's basic purpose," *cf. Great-West Life*, 534 U.S. at 220, misplaced in the context of MMS royalty collection efforts. Only in 1996, with the passage of RSFA, did Congress provide repose to federal lessees from administrative orders to collect royalties for periods longer than seven years. *See* Section II.B, *supra*.

### C. The Self-Reporting of Royalties by Oil and Gas Companies Instructs Against Implied Repose.

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[14] Dual accounting is a valuation method required in Indian leases. The lessee must calculate both (1) the value of the unprocessed gas and (2) the combined values of the processed gas and separated liquids after processing (less allowed processing costs), and pay royalties as a percentage of the higher of the two values. 30 C.F.R. § 206.155 (1988); *see also* 30 C.F.R. § 206.171 (2005).

Oil and gas companies make royalty payments to MMS based on *their own* reports of the volume and the value of their production, including their own sales to different units of the same company. *See, e.g.*, 30 C.F.R. part 210 (2005). MMS cannot be assured of the accuracy of these reports without conducting audits, *see generally* 30 U.S.C. §§ 1701, 1711; 30 C.F.R. §§ 217.50 - 217.52 (2005), which often are complex and time-consuming. Thus the companies are in full possession of all the facts concerning the amount of royalties due, whereas MMS must review production reports, sales data, company affiliations, transportation and processing costs, and other information before it can determine the amount of royalties actually due and issue an order to that effect. *See Union Texas Petroleum*, 153 IBLA at 179; *BHP Petroleum (Americas) Inc.*, 124 IBLA 185, 187-88 (1992) (cases describing the audit process).

Indeed, in enacting FOGRMA, Congress found that the oil and gas industry has operated "essentially on an honor system," without sufficient verification of industry reporting. H.R. Rep. No. 97-859, at 15. A fundamental purpose of FOGRMA was to ensure collection of the proper amount of royalties, not to protect lessees against claims for royalty payments that are still owing because of the lessees' initial underreporting and underpayment. 30 U.S.C. §§ 1701 (purposes), 1711 (directing Interior to establish, *inter alia*, "a comprehensive inspection, collection and fiscal and production accounting and auditing system to provide the capability to accurately determine oil and gas royalties . . . and to collect and account for such amounts in a timely manner"); *see also Oxy USA, Inc. v. Babbitt*, 268 F.3d 1001, 1013 (10th Cir. 2001) (Brisco, J., dissenting). Tellingly, as stated previously, *supra* at note 6, the only statute of limitations in FOGRMA when it was enacted pertained to actions to recover *penalties* under the Act. 30 U.S.C. § 1755.

These facts point to the need not for a stricter period of repose but, on the contrary, for allowing the government sufficient time to perform the necessary audits. The audit process, including the required notice to the company and opportunity to respond, *see, e.g.*, 30 C.F.R. § 217.50, is necessarily retroactive and requires a sufficient amount of time to determine whether back-royalties are due to the federal government or tribal lessors. Such detailed determinations, together with the demand for additional payment and the oil companies' administrative appeals, may take more than six years to complete, as they did in this case. *See* Pet. Br. at 8.

## IV. The D.C. Circuit's Interpretation of Section 2415(a) is Consistent with the Purposes of MMS Oversight and Avoids Unnecessary and Inefficient Litigation.

MMS has not always fulfilled its intended role of aggressive and effective royalty oversight. *See, e.g.*, Final Report on an Audit of the Minerals Management Service Audit Offices, OIG 2003-I-0023 (Mar. 31, 2003).[15] Nonetheless, states and tribes rely on MMS's authority in royalty enforcement and collection. *See generally* 30 U.S.C. §§ 1711, 1751(a); 30 C.F.R. § 201.100; *Shoshone Indian Tribe v. United States*, 58 Fed. Cl. 77, 82 (2003) (noting the Secretary's royalty collection and enforcement obligations under FOGRMA). States and tribes have taken advantage, for example, of their explicit ability under FOGRMA to identify to MMS certain leases or companies for audit, as the State of New Mexico did in the instant case. *See* 30 U.S.C. §§ 1711(c), 1732, 1735; Pet. Br. at 8. Tribes in particular, with generally fewer resources than the states, rely on MMS to perform its royalty enforcement

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[15] Available at http://www.doioig.gov.

duty consistent with the United States' trust responsibility, and both tribes and states rely on the MMS's general duty "to obtain for the public a reasonable financial return on assets that 'belong' to the public" in its role as "the statutory guardian of [the] public interest." *California Co. v. Udall*, 296 F.2d 384, 387-88 (D.C. Cir. 1961).[16]

An MMS order for additional royalty payment is one step in the process of MMS royalty enforcement. Oil- and gas-producing companies must fill out regular production and

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[16] Royalties from mineral production are one of the major sources of government revenues. *See, e.g.*, Final Report on an Audit of the Minerals Management Service Audit Offices, OIG 2003-I-0023 (March 31, 2003), at 1, available at http://www.doioig.gov ("MMS collects about $6 billion annually in rents, royalties, and other payments"); *see also* H.R. Rep. No. 106-1053, at 296-300 (2001) (recognizing that "[r]oyalties from oil and gas leases on Federal lands are one of the largest sources of non-tax revenues for the Federal Government;" that "[a]ccording to the [MMS], since 1982, nearly $100 billion has been disbursed from Federal onshore and offshore leases;" that in 1998 "the Royalty Management Program generated nearly $6 billion from more than 26,000 mineral leases," and "[o]f that amount, $550 million was distributed to the States and used for schools, roads, and public buildings;" and therefore concluding that "Congressional oversight into the management of this program. . . [is] essential to ensure a fair return to the American taxpayer" and that "[o]versight of the [DOI's] management of the valuation, collection and distribution of royalties from leases on tribal lands is also essential to ensure that the Federal Government is meeting its fiduciary responsibility as trust manager for the beneficiaries of these royalties"); H.R. Rep. No. 104-667, at 46-47 (stating that Congress enacted FOGRMA to "tighten[] the government's grip on hundreds of millions of dollars in revenue previously lost or stolen;" recognizing that "[a]ccording to the bipartisan Linowes Commission in its 1981 report, the program was losing between $200 million and $500 million annually due to theft and royalty underpayments by federal lessees;" finding that "[t]oday [1996] the program raises close to five billion dollars annually and has raised a total of $81 billion since 1982, including more than $1.5 billion in underpayments;" and concluding that "[o]nly taxes and customs raise more revenues for the U.S. Treasury").

royalty forms and submit these to MMS. *See* 30 C.F.R. §§ 210.10, 210.50-.55, 216.50-55. Based on these submissions, as well as information from states or tribes, MMS may require additional reports or subject certain leases or companies to an audit, with full notice. 30 C.F.R. §§ 210.55, 217.50. MMS may issue a Notice of Noncompliance with statutory, regulatory, or lease provisions, allowing time for correction or a hearing before assessing penalties. 30 C.F.R. §§ 241.51-.56. (2005). MMS may also issue an order for payment, as it did in this case, which is also subject to appeal. 30 C.F.R. §§ 290.102, 290.103 (2005). During this process, there is constant interaction with the oil or gas company. In the instant case, for example, an "Issue letter" was sent to Amoco on November 16, 1995, identifying under-reporting problems which affected the royalty due. J.A. at 512 (*Amoco Production Co. v. Baca*, Nos. 00-02933, 00-01480 (D.D.C.)). Further information and documentation was requested from Amoco on May 20, 1996. *Id.* at 515. MMS issued its order for additional royalties on May 27, 1997. Pet. Br. at 8. Amoco appealed administratively under 30 C.F.R. part 290. Pet. Br. at 9. Amoco then filed suit in federal court only after obtaining an unfavorable decision on appeal to the Assistant Secretary. *Id.*[17]

Due to the tribal exemption in RSFA, applying the six-year statute of limitations to MMS orders to pay royalties would upset this administrative scheme for tribes in particular,

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[17] In this case, the State of New Mexico exercised its option under FOGRMA to carry out MMS investigation and audit tasks on its own. 30 U.S.C. §§ 1732, 1735. MMS also may delegate to states the authority to issue orders to pay royalties, pursuant to 30 U.S.C. § 1734, although it has never done so. Regardless, some states and tribes may not wish or may not be able to step into the shoes of MMS pursuant to these FOGRMA provisions, and MMS ultimately is responsible for enforcement, *see generally* 30 U.S.C. § 1711, 30 C.F.R. § 229.100(b) (2005), and for administrative reviews, 30 C.F.R. part 290.

virtually eliminating a major avenue of recourse for tribes to recover royalty underpayments without going to court. If tribes could not rely on the sometimes lengthy MMS procedure, this would impose on tribes extensive auditing and fact-finding duties, as opposed to Congress' intended system through FOGRMA, in which tribes and states have the *option* of pursuing their own investigations and audits and then submitting these to MMS for enforcement. *See, e.g.*, 30 U.S.C. §§ 1732, 1735. This result not only would be unjust to the tribes who rely on MMS to carry out its fiduciary duties, but also would be contrary to the purposes of FOGRMA and the trust obligations it imposes on MMS.

Moreover, if the six-year statute of limitations in Section 2415 applied to MMS audit procedures, tribes would be forced to file otherwise unnecessary or premature claims in court to preserve their rights to royalties rather than wait for a final MMS royalty order, since the process which results in an MMS order could take more than six years. Finally, a holding that Section 2415 applies to MMS orders would encourage breach of trust lawsuits *against* the United States for failure to timely initiate collections.[18]

## CONCLUSION

The Court should uphold the decision of the U.S. Court of Appeals for the D.C. Circuit.

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[18] With the enactment of FOGRMA, Congress exhorted MMS to fulfill its trust obligations to administer oil and gas royalties, *see, e.g.*, 30 U.S.C. § 1701, and "beneficiaries of a trust are permitted to rely on the good faith and expertise of their trustees," *Wolfchild v. United States*, 62 Fed. Cl. 521, 547 (2004) (quoting *Shoshone Indian Tribe v. United States*, 364 F.3d 1339, 1347 (Fed. Cir. 2004), *cert. denied* 554 U.S. 973 (2005)).

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(5)

No. 05-669

In The
# Supreme Court of the United States

BP AMERICA PRODUCTION COMPANY
and ATLANTIC RICHFIELD COMPANY,

*Petitioners,*

v.

REBECCA W. WATSON, Assistant Secretary of
the Interior for Land and Mineral Management, *et al.*,

*Respondents.*

**On Writ Of Certiorari To The
United States Court Of Appeals
For The District Of Columbia Circuit**

## *AMICUS CURIAE* BRIEF OF MOUNTAIN STATES LEGAL FOUNDATION IN SUPPORT OF PETITIONERS

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## QUESTION PRESENTED

Whether – contrary to the decision below, but consistent with the decisions of the Tenth and Federal Circuits – the limitations period in 28 U.S.C. § 2415(a) applies to federal agency orders requiring the payment of money claimed under a lease or other agreement?

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## *AMICUS CURIAE* BRIEF OF MOUNTAIN STATES LEGAL FOUNDATION IN SUPPORT OF PETITIONERS

Mountain States Legal Foundation ("MSLF") respectfully submits this *amicus curiae* brief in support of Petitioners. Pursuant to Supreme Court Rule 37(2)(a), this *amicus curiae* brief is filed with the written consent of all the parties.[1]

## IDENTITY AND INTEREST OF *AMICUS CURIAE*

MSLF is a non-profit, public interest legal foundation organized under the laws of the State of Colorado. MSLF is dedicated to bringing before the courts those issues vital to the defense and preservation of private property rights, individual liberties, limited and ethical government, and the free enterprise system. MSLF's members include businesses and individuals who live and work in nearly every state of the country.

Many of MSLF's members own natural gas operations pursuant to federal leases that are subject to royalty payments like those at issue in this case. Because MSLF and its members have a significant interest in the outcome of this case, MSLF respectfully submits this brief in support of Petitioners.

[1] A copy of Respondents' consent letter has been filed with the Clerk of the Court; and Petitioners filed a blanket consent. In compliance with Supreme Court Rule 37(6), MSLF represents that no counsel for any party authored this brief in whole or in part and that no person or entity, other than the *amicus curiae*, its members, or its counsel made a monetary contribution to the preparation or submission of this brief.

## OPINIONS BELOW AND JURISDICTION

*Amicus* hereby adopts Petitioners' description of the opinions below and statement of jurisdiction. *See* Petition for Writ of *Certiorari* at 1-14.

## STATEMENT OF THE CASE

In 1920, Congress enacted the Mineral Leasing Act ("MLA"), 30 U.S.C. § 181, *et seq.*, to authorize the U.S. Department of the Interior ("DOI") to issue and administer oil and gas leases for federal lands. 30 U.S.C. §§ 181-287. To operate oil and gas leases on federal lands, lessees are required to pay a royalty to the Mineral Management Service ("MMS"), a division of the DOI, that is based on the value of the gas.

Petitioners own such leases and have consistently been subject to the royalty payment requirement. On April 22, 1996, the MMS issued a "Dear Operator/Payor" Letter to producers of coalbed methane ("CBM") gas in the vicinity of New Mexico's San Juan Basin. The 1996 Payor Letter provided new "guidelines" to producers on how to report and pay these royalties. Specifically, the MMS claimed a royalty entitlement based on the enhanced value of CBM after transportation to downstream treatment facilities and treatment in those facilities to meet mainline pipeline quality requirements. The 1996 Payor Letter asserted that, for royalty purposes, the CBM's "value" may not be reduced to account for the costs of placing it in marketable condition, and that the CBM was not in marketable condition until it was transported to and treated in gas treatment plants to meet the quality specifications of mainline pipelines.

On May 27, 1997, the MMS issued an order directing Petitioners to pay additional royalties of $4,117,607 because, according to the MMS, Petitioners had calculated and paid royalties improperly dating back to 1989. The order also imposed penalties of up to $10,000 per day for failure to comply with the order.

Petitioners believe that such a demand violates 28 U.S.C. § 2415(a), which provides, in part:

> Subject to the provisions of section 2416 of this title, and except as otherwise provided by Congress, every action for money damages brought by the United States or an officer of agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later . . .

This statute of limitations was not included initially in the MLA, but was added in 1966 and then amended in 1982 to include the phrase, "[t]he provisions of this section shall not prevent the United States or an officer or agency thereof from collecting any claim of the United States by means of administrative offset, in accordance with section 3716 of title 31." 28 U.S.C. § 2415(i).

After exhausting administrative remedies, Petitioners filed suit in the United States District Court for the District of Columbia, which concluded that the statute of limitations does not apply to agency efforts to impose and collect additional royalties through agency proceedings. *Amoco Production Co. v. Baca*, 300 F.Supp.2d 1, 21 (D.D.C. 2003).

The United States Court of Appeals for the District of Columbia affirmed this decision, holding that "an administrative order assessing additional royalties" cannot reasonably be understood to be an "action for money damages" initiated by the filing of a complaint. *Amoco Production Co. v. Watson*, 410 F.3d 722 (D.C. Cir. 2005). Thereafter, Petitioners filed their Petition for Writ of *Certiorari* with this Court, which was granted on April 17, 2006.

## SUMMARY OF THE ARGUMENT

Agency orders, such as the MMS's order to Petitioners, fall within the plain meaning of 28 U.S.C. § 2415(a), and, therefore, this Court should reverse the holding of the D.C. Circuit Court. This conclusion is supported by this Court's doctrine that eschews absurd results, such as concluding that administrative agencies may attempt to collect money though the administrative process while being barred from collecting that money through litigation. In addition, the D.C. Circuit wrongly adhered to a canon of construction, which provides that statutes of limitations are to be strictly construed in favor of the government, that is inapplicable both in this specific instance and universally. As a result, this Court should reverse the decision of the D.C. Circuit and hold that administrative orders do fall within the purview of the statute of limitations.

## ARGUMENT

Statutes must be interpreted based on the plain meaning of the statutory text. *Barnhart v. Sigmon Coal*

*Co., Inc.*, 534 U.S. 438, 450 (2002) ("As in all statutory construction cases, we begin with the language of the statute."); *Stenberg v. Carhart*, 530 U.S. 914, 983 (2000) (Scalia, J., concurring in judgment in part and dissenting in part). "In ascertaining the plain meaning of [a] statute, the court must look to the particular statutory language at issue, as well as the language and design of the statute as a whole." *K Mart Corp. v. Cartier, Inc.*, 486 U.S. 281, 291 (1988). The textual canon *in pari materia* may be applied to aid in the construction of the statutory text by examining the language and design of the statute as a whole. Under this doctrine, "if divers statutes relate to the same thing, they ought all to be taken into consideration in construing any one of them." *Branch v. Smith*, 538 U.S. 254, 281 (2003), citing *U.S. v. Freeman*, 3 How. 556, 564-565, 11 L.Ed. 724 (1845). If, however, the plain meaning of the statutory text would lead to an absurd result, this Court has concluded that other factors may be taken into consideration. *See, e.g., Watt v. Alaska*, 451 U.S. 259, 285 n.8 (1981).

This case hinges on the interpretation of 28 U.S.C. § 2415(a):

> Subject to the provisions of section 2416 of this title, and except as otherwise provided by Congress, every action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or law, whichever is later. . . .

To determine the applicability of this statute to Petitioners, the D.C. Circuit affirmed the District Court's decision in favor of the MMS because it concluded that "the government's demand for additional royalties is not an action for money damages initiated by the filing of a complaint." *Amoco Production Co.*, 410 F.3d at 735. The court ruled in favor of the MMS, in part, because "statutes of limitations against the sovereign are to be strictly construed [in favor of the government]." *Id.* at 734; *see also E.L. DuPont de Nemours & Co. v. Davis*, 264 U.S. 456, 462 (1924) (In the absence of congressional enactment clearly imposing a statute of limitations on the government, a statute of limitations is to be strictly construed in favor of the government.).

Here, a textual interpretation of the plain meaning of the statute, aided by the canon *in pari materia*, mandates that this Court reverse the opinion below. This Court's precedent, which eschews absurd results, supports this conclusion, particularly when the statute of limitations is fairly and reasonably construed.

## I. THE TEXT OF 28 U.S.C. § 2415(a) PLAINLY MEANS, WHEN AIDED BY THE CANON *IN PARI MATERIA*, THAT AGENCY ORDERS FALL WITHIN THE PURVIEW OF THE STATUTE OF LIMITATIONS.

The plain meaning of 28 U.S.C. § 2415(a), when aided by the canon *in pari materia*, is unambiguously clear: administrative orders fall within the purview of the statute of limitations. Any statutory construction begins with its plain meaning. *Barnhart*, 534 U.S. at 450. This analysis requires a careful examination of both the statutory text, as well as the "language and design of the

statute as a whole." *K Mart Corp.*, 486 U.S. at 291. This Court has applied the textual canon *in pari materia* to help interpret the language and design of the statute as a whole. Under this doctrine, "if divers statutes relate to the same thing, they ought all to be taken into consideration in construing any one of them." *Branch*, 538 U.S. at 281, citing *U.S. v. Freeman*, 3 How. 556, 564-65, 11 L.Ed. 724 (1845). Further, the various provisions within one statute should all be taken into account when interpreting a statute. *See, e.g., U.S. v. Riverside Bayview Homes, Inc.*, 474 U.S. 121, 139 n.11 (1985). Applying this principle, "when Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion." *Barnhart*, 534 U.S. at 452 (internal citations omitted).

An amendment to the statute, 28 U.S.C. § 2415(i), expressly exempts administrative offsets from the statute of limitations period set forth in 2415(a). An "administrative offset" is not a judicial action. Therefore, if § 2415(a) were limited solely to judicial actions, there would have been no need to legislate a specific exemption for administrative offsets, and such an exemption would yield statutory surplusage, which is disfavored by this Court. *See, e.g., U.S. v. Menasche*, 348 U.S. 528, 538-39 (1955). Notably, the doctrine of *in pari materia* mandates that § 2415(i) be used to help interpret § 2415(a). Therefore, "[e]xamination of the language and the structure of section 2415 leaves the conviction that, absent an express exception, Congress intended that agencies assert their claims within six years or lose the right to enforce them." *U.S. v. Hanover Insurance Co.*, 82 F.3d 1052, 1055 (Fed. Cir. 1996).

## II. THE HOLDING OF THE D.C. CIRCUIT COURT OF APPEALS YIELDS AN ABSURD RESULT AND OUGHT TO BE REVERSED.

This Court's precedent that eschews absurd results further leads to the conclusion that the decision below should be reversed. The MMS's order, dated May 27, 1997, demands royalty payments of $4,117,607. It also warns that failure to pay such royalty payments could result in penalties of up to $10,000 per day. Petition for Writ of *Certiorari*, Appendix H. Should Petitioners refuse to make any royalty payments older than six years, the MMS would likely have to file a complaint with a court to collect this money.

Oil and gas leases have long been recognized as "contracts." *See, e.g., OXY USA, Inc. v. Babbitt*, 268 F.3d 1001, 1006 (10th Cir. 2001). Furthermore, an award of "damages" is the relief sought as a result of a breach of contract. *See, e.g., id.* at 1008 (referencing *Farnsworth on Contracts* § 12.8, at 871 (2d ed. 1990)). Therefore, for the MMS to collect, the complaint would have to allege a breach of contract resulting in money damages.

Once the complaint is filed to collect the royalties, the statute of limitations would bar any claim for contract damages beyond the six-year limitations period. By holding that the statute of limitations does not apply to agency actions, the D.C. Circuit's decision effectively permits the MMS to attempt administratively what it would be unable to accomplish judicially. This inconsistency could not possibly have been the intent of Congress in enacting 28 U.S.C. § 2415(a), the purpose of which was to "establish a general statute of limitations on contract claims asserted

by the government or a government agency." *OXY USA, Inc.*, 268 F.3d at 1005. "An interpretation of § 2415 permitting federal agencies to avoid the limitation period by utilizing administrative orders to collect monies owed under contract obviously would thwart this purpose." *Id.* at 1006.

A similarly absurd result would exist if the MMS were to file a complaint to compel Petitioners to pay only the penalties for noncompliance. Though, theoretically, the statute of limitations for the penalties would begin to run the moment the penalties were assessed, it makes little sense to permit the MMS to collect penalties for failure to make a payment that the MMS is barred from collecting. Such a result would not give the parties finality on stale claims. Because this result would be absurd, this Court's own precedent suggests that § 2415(a) should be interpreted more reasonably.

## III. THE STATUTE OF LIMITATIONS, 28 U.S.C. § 2415(a), SHOULD NOT BE STRICTLY CONSTRUED IN FAVOR OF THE GOVERNMENT.

When statutes are ambiguous, this Court has relied occasionally upon other methods of construction, such as legislative intent and non-textual canons of construction. *See, e.g., Household Credit Services, Inc. v. Pfennig*, 541 U.S. 232 (2004) (courts must give effect to the unambiguously expressed intent of Congress); *Connecticut Nat. Bank v. Germain*, 503 U.S. 249, 253-54 (1992) (legislative history and other canons of construction are useful interpretive tools when a statute is ambiguous). Here, these

additional construction tools further support the conclusion that the decision below should be reversed.

Though this Court should conclude that the plain meaning of the statute unambiguously includes administrative orders, the D.C. Circuit relied, in part, on the canon of construction that provides that statutes of limitations should be strictly construed in favor of the government. First, this canon conflicts with the intent of Congress, and, therefore, should not be applied in this instance. Second, the foundation underlying this canon is weak and the canon ought to be overturned in all instances.

### A. The Purpose Of The Canon Of Construction Was Rejected By Congress When 28 U.S.C. § 2415(a) Was Debated, Thus The Canon Ought Not Be Applied In This Instance.

Statutes of limitations exist to prevent limitless and open-ended liability, *see generally* Victor E. Schwartz, *et al.*, *Prosser, Wade & Schwartz's Torts Cases and Materials* 613-619 (10th ed. 2000), and to provide finality to parties' legal obligations and relations, including contracts with the government, as recognized by § 2415(a).[2] This Court

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[2] *See also Bell v. Morrison*, 26 U.S. (1 Pet.) 351, 360 (1828) (Story, J.) (statutes of limitations guard against "stale demands, after the trust state of the transaction may have been forgotten."); *Walker v. Armco Steel Corp.*, 446 U.S. 740, 751 (1980) ("The statute of limitations establishes a deadline after which the defendant may legitimately have peace of mind; it also recognizes that after a certain period of time it is unfair to require the defendant to attempt to piece together his defense to an old claim."); *Order of Railroad Telegraphers v. Railway Express Agency, Inc.*, 321 U.S. 342, 348-49 (1943) (statutes of limitations "promote justice by preventing surprises through the revival of claims

(Continued on following page)

has concluded that "it is obvious that [statutes of limitations] are an integral part of the legal system and are relied upon to protect the liabilities of persons and corporations active in the commercial sphere." *Bendix Autolite Corp. v. Midwesco Enterprises, Inc.*, 486 U.S. 888, 893 (1988).

Statutes of limitations also serve valid legal purposes:

> Statutes of limitations are not simply technicalities. On the contrary, they have long been respected as fundamental to the well-ordered judicial system . . . The process of discovery and trial . . . is obviously more reliable if the witness or testimony in questions is relatively fresh. Thus . . . there comes a point at which the delay of a plaintiff in asserting a claim is sufficiently likely either to impair the accuracy of the fact-finding process or to upset the settled expectations that a substantive claim will be barred . . .

*Board of Regents of University of State of N.Y. v. Tomanio*, 446 U.S. 478, 486 (1980).

Balanced against these valid, important purposes of statutes of limitations is the canon of construction that provides that, in the absence of a congressional enactment, such statutes are to be strictly construed in favor of the government. The purpose for such a canon was to protect the public from the prejudice that could result from the negligence of governmental officers in their untimely filing of claims. *U.S. v. Nashville, C. & St. L. Ry. Co.*, 118 U.S. 120 (1886).

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that have been allowed to slumber until evidence has been lost, memories have faded, and witnesses have disappeared.").

With regard to § 2415(a), however, this public purpose was rejected by Congress, which enacted § 2415(a) "to promote fairness . . . notwithstanding whatever prejudice might accrue thereby to the Government as a result of the negligence of its officers." *Hanover Insurance Co.*, 82 F.3d at 1055. Therefore, specifically with regard to § 2415(a), the canon ought to be rejected, and the statute should not be strictly construed in favor of the government. *See, e.g.*, *Smith v. City of Jackson, Miss.*, 544 U.S. 228, 262 (2005) (Rehnquist, J., dissenting from denial of *certiorari* to, instead, expressly affirm the decision, below) ("Even venerable canons of construction must bow, in an appropriate case, to compelling evidence of congressional intent."); *South Carolina v. Catawba Indian Tribe, Inc.*, 476 U.S. 498, 507 n.16 (1986) ("A canon of construction is not a license to disregard clear expressions of . . . congressional intent."). Instead, the aforementioned justifications warrant a statutory interpretation whereby the protections provided by the statute are not limited by the canon of construction in favor of the government.

### B. The Canon Of Construction Whereby Statutes Of Limitations Are To Be Strictly Construed In Favor Of The Government, Is Illogical And Should Not Be Applied Under Any Circumstances.

"The doctrine of *stare decisis* is essential to the respect accorded to the judgments of this Court and to the stability of the law," *Lawrence v. Texas*, 539 U.S. 558, 577 (2003) (wherein the Court expressly overruled *Bowers v. Hardwick*, 478 U.S. 186 (1986)). However, that doctrine is "not an inexorable command []." *Dickerson v. U.S.*, 530 U.S.

428, 443 (2000) (quoting *State Oil Co. v. Khan*, 522 U.S. 3, 20 (1997) (expressly overruling *Albrecht v. Herald Co.*, 390 U.S. 145 (1968)); *Agostini v. Felton*, 521 U.S. 203, 235 (1997) (abandoning a strict application of *stare decisis*). Instead, it is a mere "principle of policy." *Lawrence*, 539 U.S. at 577. Therefore, "[i]n prior cases, when this Court has confronted a wrongly decided, unworkable precedent calling for some further action by the Court, [the Court has] chosen not to compound the original error, but to overrule the precedent." *Payne v. Tennessee*, 501 U.S. 808 (1991) (Souter, J., concurring) (wherein the Court partially overruled *Booth v. Maryland*, 482 U.S. 496 (1987) and *South Carolina v. Gathers*, 490 U.S. 805 (1989)). The canon of construction upon which the D.C. Circuit partially relied, which provides that statutes of limitations are to be strictly construed in favor of the sovereign, is absurd and poorly reasoned and ought to be overruled.

Many statutes of limitations are imposed by the legislature on individuals. *See, e.g.*, 28 U.S.C. § 2244(d)(1) (imposing a statute of limitations on the filing of a *habeas corpus* petition). These statutes, which limit the rights of action available to individuals, are not strictly construed in favor of the individual, despite that the individuals had no influence in the statutes' enactment. Yet pursuant to the canon of construction, statutes that limit the rights of action available to the government are strictly construed in favor of the government even though the limitation is self-imposed.

This makes little sense. Because Congress has the power to protect itself from the limitations imposed by a statute of limitations, it can repeal an enacted statute of limitations or reject it before it becomes law. In other words, should Congress believe that a particular statute of

limitations overly restricts the rights of the government to seek redress, Congress may amend or repeal that statute. Individuals, on the other hand, have no such power. Therefore, the canon that provides for a strict construction of statutes of limitations in favor of the government cannot be justified.

A similar theory, known as "*contra proferentem*," is commonly applied in contract law, though it has been used occasionally in statutory construction. *See, e.g., Germantown Pass. Ry. Co. v. Citizens' Pass. Ry. Co.*, 24 A. 1103, 1104, 151 Pa. 138, 140 (Pa. 1892); Larry A. DiMatteo, *Equity's Modification of Contract: An Analysis of the Twentieth Century's Equitable Reformation of Contract Law*, 33 New Eng. L. Rev. 265, n.584 (Winter 1999) ("The concept of strict construction against the drafter can be found throughout Anglo-American Jurisprudence in both statutory and non-statutory interpretations."). The doctrine provides that "In interpreting documents, ambiguities are to be construed unfavorably to the drafter," Black's Law Dictionary 328 (7th ed. 1999); *see also* Restatement (Second) of Contracts § 206 (1981), "because the drafter is the party in a position to correct the ambiguity." *Gunn v. Principal Cas. Ins. Co.*, 605 So.2d 741, 746 (Miss. 1992); *see also U.S. v. Seckinger*, 397 U.S. 203, 216 (1970) (doctrine of *contra proferentem* is given "considerable emphasis" in construing a government contract "because of the government's vast economic resources and stronger bargaining position."). Following this same reasoning, an ambiguous statute of limitations that restricts the right of the government to seek redress should not be strictly construed in favor of the government and, if anything, should be strictly construed against the government.

Ultimately, such a canon of construction, which creates preferential rules and presumptions, obfuscates the statutory interpretation process. "It is hard enough to provide a uniform, objective answer to the question whether a statute, on balance, more reasonably means one thing than another. But it is virtually impossible to expect uniformity and objectivity when there is added, on one or the other side of the balance, a thumb of indeterminate weight." Antonin Scalia, *A Matter of Interpretation: Federal Courts and the Law* 28 (Princeton University Press 1997). Given these considerations, this Court should reject the canon of construction that mandates a strict construction of statutes of limitations in favor of the government, and reverse the decision below.

## CONCLUSION

Agency orders, such as the MMS's order to Petitioners, fall within the purview of 28 U.S.C. § 2415(a), when textually construed, and therefore this Court should reverse the holding of the D.C. Circuit Court. This "plain meaning" interpretation is supported by this Court's doctrine that eschews absurd results. Here, the D.C. Circuit Court's conclusion that the text of § 2415(a) places a time limitation only on judicial actions leads to an absurd result whereby an administrative agency could attempt to collect money though the administrative process while being barred from judicial enforcement of this administrative decision. Additionally, a reversal is supported both by the purpose of § 2415(a) and by logic, which mandates that this Court reject the canon of construction, which construes statutes of limitation in favor of the government, that underlies the erroneous decision of

the court below. Therefore, Mountain States Legal Foundation respectfully requests that this Court reverse the decision of the D.C. Circuit Court and hold that § 2415(a) does apply to administrative orders.

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